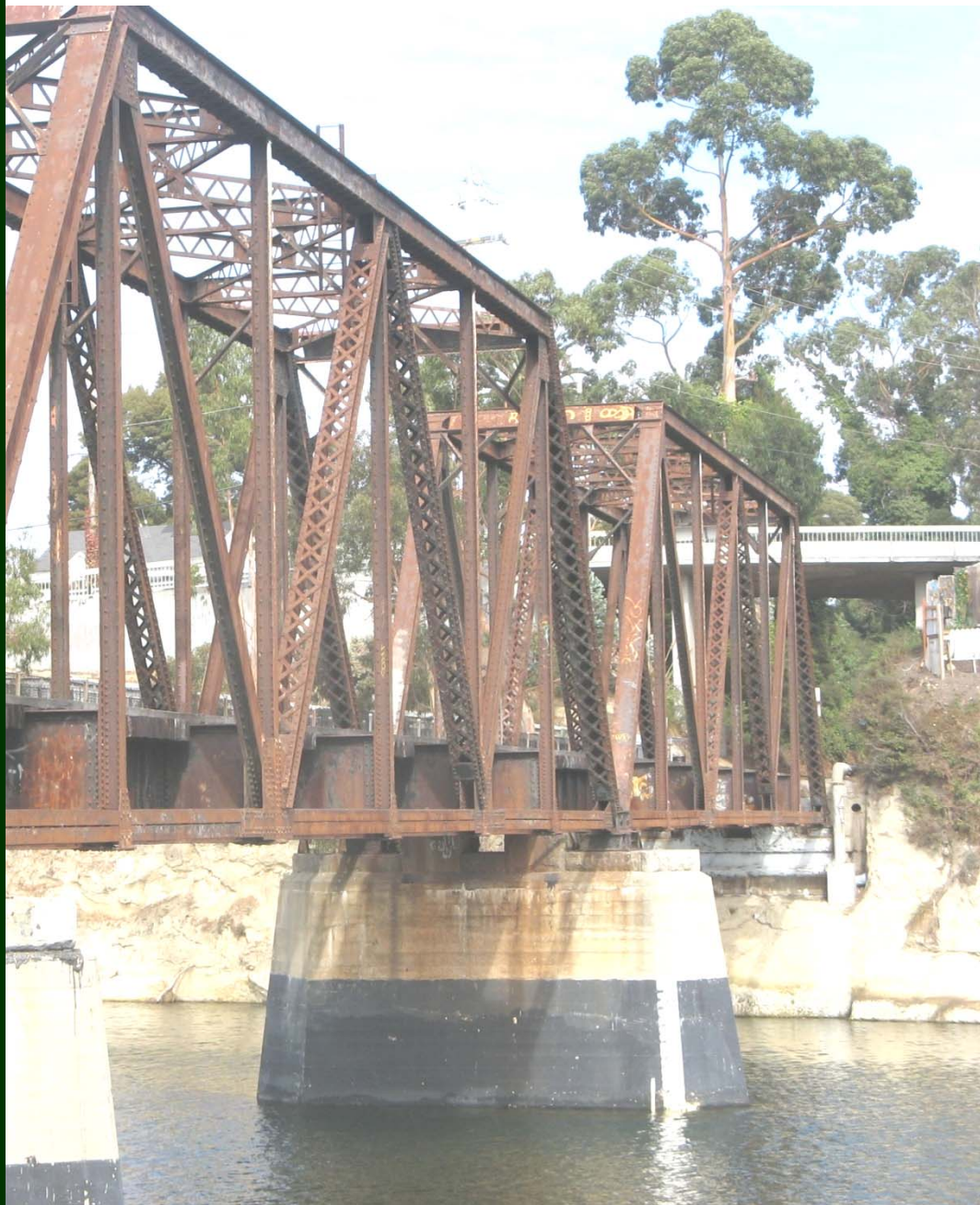


Draft
December 2008

Business and Management Plan

SCCRTC Rail Line Assets

Renaissance Rail Group
Egan Consulting Group



Disclaimer

The analysis contained in this Plan has been developed from information gathered from third party sources. The authors make no warranty as to the accuracy or completeness of information received from or through such sources.

Additionally, this Plan has relied on both proprietary information and modeling tools to filter and evaluate the information gathered.

Glossary of Terms

Abandonment: In railroad abandonment, a railroad serves notice that it will cease operating all or part of a route or service, especially with the intent of never resuming it again. (If the route may possibly reactivate at some point in the future, then a separate process called railbanking is used.) It is a defined process, starting with a railroad's petition to the Surface Transportation Board (STB) in Washington, DC, the Federal regulatory agency that oversees the activities of railroads, trucking companies, and intercity bus companies. Abandonment can only occur with the permission of the STB, after the board considers the need of local communities and shippers for continued service balanced by the broader public interest in freeing railroads from financial burdens that are a drain on their overall financial health and lessen their ability to operate economically elsewhere.

Car Hire: Rate paid to the owner of a railroad car while that car is not on owner's property. Car Hire is typically charged in two components – an hourly charge and a mileage charge.

Car Supply: The availability of specific types of rail cars to meet specific customer requirements. Typically, a railroad will provide the necessary equipment on behalf of the customer and the transportation rate it charges is inclusive of providing this equipment. In the event the railroad cannot, or chooses not to provide equipment, it is up to the customer or a third party to provide the necessary rail equipment.

Common Carrier: A common carrier holds itself out to provide service to the general public without discrimination for the "public convenience and necessity". A common carrier must further demonstrate that it is "fit, willing and able" to provide those services for which it is granted authority.

Demurrage: In railroad application, it is the charge on detention of rolling stock, either to the shipper for holding the car (laden or not), or to the connecting railroad(s) while the car is empty and returning to the home road, in either case, as a way to encourage speedy unloading and return of empties to improve utilization of rolling stock.

EBITDA: "Earnings Before Interest, Taxes Depreciation and Amortization" is a non-GAAP metric that can be used to evaluate a company's profitability. EBITDA differs from the operating cash flow in a cash flow statement primarily by excluding payments for taxes or interest as well as changes in working capital. EBITDA also differs from free cash flow because it excludes cash requirements for replacing capital assets (CAPEX). EBITDA is used when evaluating a company's ability to earn a profit.

Handling Carrier: A Handling Carrier is a specific compensation structure applied to a railroad operating on behalf of a larger (typically Class 1) railroad in a defined railroad corridor. The railroad operates "as if" it were the larger (Class 1) railroad in most commercial aspects.

Offer of Financial Assistance (OFA): An OFA is submitted to the Surface Transportation Board during a rail abandonment proceeding, and allows a financially responsible party to submit a financial plan for continued operation of rail line assets proposed to be abandoned.

Revenue Allowances: Revenue or Handling Carrier Allowances are per car rates paid by a Class 1 Railroad to a shortline railroad operating on the Class 1's behalf over designated rail lines.

Temporal Separation: Defining specific or distinct times of day / days of week and specific boundaries under which various operational activities can take place, and wherein no cross-over of these activities takes place.

Trackage Rights: Contractual agreement between railroads whereby one railroad may operate, for convenience or necessity-sake over the tracks of another railroad. Trackage Rights agreements may be permanent or temporary.

Table of Contents

Section 1: Executive Summary	4
Section 2: Analysis of Current Operations	17
Section 3: Transaction Options for New Shortline Railroad Operations	24
Section 4: New Shortline Railroad Operations	37
Operating Plan	37
Marketing / Business Development Plan	43
Capital and Maintenance Plan	50
Financial Analysis of New Shortline Operations	54

Section 1

Executive Summary

Scope of Work

Renaissance Rail Group, Incorporated and Egan Consulting Group have been engaged by the Santa Cruz County Regional Transportation Commission (RTC) to prepare a comprehensive Business and Management Plan (“Plan”) and Financial Analysis for the 32-mile Watsonville – Davenport, CA rail corridor proposed for purchase by the RTC from the ***Union Pacific Railroad (UP)***.

Development of this Plan and Financial Analysis has encompassed several tactical activities, including:

1. Meeting with or conducting telephone interviews with customers currently utilizing rail service in the corridor to assess current rail usage, future rail usage and identify any specific issues salient to their use of rail transportation. Current customers met with include:

- a. CEMEX
- b. Lumberman’s (ProBuild)
- c. Cascade Properties (Terminal Freezers)
- d. Del Mar Food Products

These customers represent 95% of the current originating / terminating freight rail traffic in the corridor.

2. Meeting with community and regional economic development agencies to identify opportunities for expanded use of rail in the region and to uncover any specific issues and concerns with freight railroad service and the RTC’s proposed acquisition of these rail line assets. Agencies met with include:

- a. Santa Cruz County Redevelopment Agency and Planning Department
- b. City of Santa Cruz:
 - i. Economic Development
 - ii. Redevelopment Department
 - iii. Public Works Department
- c. City of Watsonville
 - i. Community Development Department
 - ii. Redevelopment and Housing Department

3. Identifying and interviewing potential new users of freight rail service in the region. Potential new users of freight rail service identified to date include:

- a. Graniterock
- b. City of Santa Cruz Public Works Department

- c. Constituent members of the Grower-Shipper Association of Central California
4. Identifying general potential opportunities that can be pursued to increase freight rail volumes in the corridor
5. Review of documents related to proposed and potential Transaction Structures for the acquisition of the corridor and the establishment of shortline railroad operations therein.
6. Review of existing Engineering and Business Plan work done on behalf of the RTC over the last several years related to its proposed acquisition of the railroad corridor.¹²
7. Physical inspection of the rail line from Watsonville to Davenport.

Confidential Information

Information provided by current customers with respect to the details of their use of freight rail services has been collected and used in the development of this Plan. Certain portions of this information are general in nature and easily obtained through public means and general observation, while other components are proprietary and commercially sensitive.

Information that is considered proprietary and commercially sensitive has been provided to SCCRTC and its consultants only under terms of a formal Confidentiality Agreement, between the SCCRTC and the specific customer sharing such information.

This Draft Report is a confidential document in its entirety. At such point in time where it is made available for public review and inspection, a separate Appendix containing the Confidential and Commercially Sensitive Information in this Report will be prepared as a confidential appendix to this Plan.

Objectives of Plan

This Plan is designed to achieve the following Objectives:

1. Provide an overview of current Freight railroad operations conducted by the Union Pacific in the Watsonville – Davenport rail corridor.
2. Identify and analyze potential transaction structures with the UP and the shortline railroad operations that could result.

¹ Santa Cruz industrial Lead – Supplemental Structural Plan (6/2006) and Updated Summary of Estimated Capital and Maintenance Costs (4/2008)

² Santa Cruz Branch Line Draft Business Plan (8/2004)

3. Create a comprehensive analysis of shortline railroad operations in the Watsonville – Davenport corridor under various transactions structures to understand the financial viability of such operations.
4. Identify new opportunities to enhance the freight railroad viability of the corridor.
5. Provide a comprehensive business and management plan for the RTC's ownership of the Branch Line.

Plan Summary

Current Railroad Operations

1. UP is currently providing service to rail customers in the Watsonville – Davenport corridor up to 4 days per week.
2. Rail traffic in the corridor is concentrated primarily in Davenport at CEMEX's facility, secondarily in Watsonville, and with a smaller concentration of traffic in Santa Cruz.
3. CEMEX is the largest single shipper in the corridor. Given the density of traffic in Davenport and the service requirements necessary to support CEMEX's manufacturing operations, the railroad must operate a minimum of three days per week from Watsonville to Davenport to provide adequate service to CEMEX.
4. UP began internal initiatives to outsource freight operations in the corridor to a shortline freight railroad operator in spring 2007. The decision to outsource local freight operations is likely due to a combination of factors, including Union Pacific's desire to:
 - a. Focus resources on their core, higher density franchise;
 - b. Avoid higher than average per-mile maintenance costs unique to this rail corridor;
 - c. Avoid what appears to be higher liability risks associated with the proximity of the railroad right-of-way to high-density pedestrian venues;
 - d. Avoid future capital investment in the numerous bridges and structures along the corridor.

Shortline Freight Railroad Operation

Shortline Overview

A shortline railroad is broadly defined as a railroad that operates in a limited geographic region and focuses on providing local, "retail" transportation services to customers in that region. Most shortline railroads have been created as a "spin-off" or outsourcing by a Class 1 railroad.

Successful shortline railroads specialize in working with customers and communities to maximize the use of rail by industries in the region; they oftentimes improve service frequency, and work to attract new industry to the regions in which they provide service.

Shortline railroads connect their customers to the larger rail network and the outside world at mutually agreed upon “interchange” locations. In the specific case of the Watsonville – Davenport rail corridor, the shortline railroad would likely connect with the UP in Watsonville Yard. However, until such a transaction is agreed upon, it should only be assumed that such interchange would occur at a mutually-agreed location.

The majority of a shortline railroad’s revenue base is typically provided through a share of the freight revenue, often referred to as an “allowance” or “handling allowance” paid by the Class 1 railroad for every loaded car handled by the shortline. The amount paid per car is normally a function of the commodities carried and/or the distance the shortline must operate to serve each customer.

Low value bulk commodities generally generate lower allowances than finished goods, chemicals and other high-value items. The current commodity mix on this line segment favors lower-rated commodities.

Potential Transaction Options – Line Sale and Shortline Operations

Several potential options exist relative to the purchase of the rail corridor and the establishment of shortline rail operations. This section of the report attempts to provide sufficient information on the range of options available to the Commission to insure that an informed decision is made based on the needs of the commission and county. The potential transaction options include:

1. The UP Proposed option of a shortline operator selected by and contracted to UP;
2. A shortline operator selected by the SCCRTC as result of an RFP process, and contractually linked to the SCCRTC;
3. The SCCRTC creating an entity to operate the shortline railroad

Each of these options is discussed in more detail below. While variations of the discussed options can, and should, be considered the three options reviewed allow the Commission to consider the entire continuum of options available.

UP-Proposed

Union Pacific has suggested a general framework for a transaction structure for the sale of the rail line to RTC and the establishment of shortline railroad operations in the corridor.

While the Union Pacific has not provided specific details of a proposed transaction structure for this property, they have provided the RTC with details of what UP considers a two-fold transaction made in 2002 and 2007 with Utah Transit Authority (UTA).

In the UTA transaction, rail line assets were sold in 2002 to a transportation agency for commuter rail operations, while UP retained freight operating rights. In 2007, additional property was sold to the

UTA, and the UP elected to contract with a shortline railroad operator to provide continued freight rail service on these assets.

Salient highlights of this structure, as it relates to the proposed transaction on the line between Watsonville and Davenport, include:

1. UP proposes to select their own operator, in this case, WATCO Companies (WATCO) for freight operations in the corridor and will enter into their own separate commercial and operating agreements with WATCO for freight rail service.
2. UP may elect to install WATCO as shortline operator in the rail corridor prior to a purchase transaction occurring with the RTC.
3. Concurrent with, and as a condition of RTC's acquisition of the rail line, certain agreements between the WATCO-operated shortline and RTC would need to be established governing maintenance requirements, insurance requirements, and other non-commercial aspects of the shortline's relationship with the RTC. Such agreements would be the proper venue to address such issues as RTC's responsibility, if any, in regards to such issues as maintenance, response to catastrophic failure on the line, response to financial failure or abandonment.
4. RTC would have no responsibility for maintenance, routine or catastrophic; and would have no control over an attempt by WATCO to abandon service in the event of catastrophic loss or other events.
5. RTC would need to identify additional expectations of WATCO related to passenger rail, commuter rail and shared use of corridor for trail development and establish additional agreements with WATCO related to these expectations as necessary.
6. The UP-proposed arrangement does not contemplate the RTC sharing in any freight revenues derived from operations in the corridor (although the UTA deal did contain a limited revenue component). While the RTC has assumed all along that any additional revenues from the property (pipe and wire crossings and other occupancies) would accrue to the Commission, it would be prudent to memorialize such expectations.
7. There is no expectation that a WATCO shortline operation will receive operating subsidies from RTC to cover operating losses. WATCO may opt to abandon service, if faced with operating losses.
8. The UP appears willing to retain Residual Common Carrier Authority under their currently-proposed arrangement.

This Plan and accompanying Financial Analysis provides potential benchmark standards around which the RTC can evaluate the commercial assumptions made by UP and WATCO related to future freight operations in the corridor.

RTC- Directed: RFP for Shortline Operator

The RTC may elect to advise the Union Pacific that as part of its proposed purchase of the line it will select any shortline operator. In such a case the RTC would develop a Request for Proposal for a potential shortline operator as a condition of its proposed purchase of the Watsonville – Davenport rail line corridor from the UP. Salient issues of this structure would include:

1. RTC would select the shortline operator based upon a variety of criteria deemed important to protect RTC's ownership of, and rights in, the corridor.
2. Shortline operator would execute appropriate agreements with the RTC governing maintenance requirements, insurance requirements, as well as other aspects of the shortline's relationship with the RTC.
3. Shortline operator would be expected to begin operations in the corridor upon closing the purchase of rail line by RTC. However, certain provisions for earlier or later shortline start-up could be established if deemed necessary, convenient or required by UP.
4. S Shortline operator (possibly with assistance from the RTC) would need to negotiate and finalize necessary Commercial and Operating agreements with the UP 30-60 days prior to assuming operations in the corridor.
5. The responsibility for Residual Common Carrier Authority would need to be negotiated with UP as a component of Line Purchase transaction.
6. Shortline would not receive operating subsidies from RTC to cover operating losses and may opt to abandon service if faced with losses.
7. Shortline would have the option for covering catastrophic losses to right-of-way and structures and may opt to abandon service if faced with costly catastrophic event.

This Plan and accompanying Financial Analysis provides information and benchmark standards around which an RFP can be developed and potential shortline Proposals can be evaluated by the RTC as part of the RFP process.

Local Government Agency Ownership of Shortline Railroad

The RTC may elect as an alternative option, or as a condition of its purchase of the Watsonville-Davenport rail line and right of way assets, to own and operate the shortline freight railroad operating in the corridor through a separate public operating agency. Salient issues of this structure would include:

1. RTC will establish, through a separate public operating entity, a shortline in conjunction with its purchase of rail line and right-of-way assets.
2. The public operating agency would begin operations in the corridor upon closing the purchase of rail line by RTC. However, certain provisions for earlier or later shortline start-up could be established if deemed necessary, convenient or required by UP.
3. The public operating agency would be entitled to all freight revenues generated by shortline.
4. The public operating agency, the RTC or local taxpayers would be responsible to provide operating subsidies to cover operating losses of shortline, or opt to abandon freight service.
5. The responsibility for Residual Common Carrier Authority would need to be negotiated with UP.
6. The public operating agency, the RTC or local taxpayers will be responsible for covering catastrophic losses to right-of-way and structures or opt to abandon service.

This Plan, especially **Section 4: New Shortline Railroad Operations** and accompanying Financial Analysis provides detailed information and benchmark standards around which the RTC could establish its own shortline railroad agency in conjunction with the purchase of the Watsonville – Davenport rail corridor.

Financial Analysis of Shortline Railroad Operations

For purposes of evaluating the financial viability of shortline railroad operations in the corridor, three basic models were developed:

1. Shortline railroad start-up as a subsidiary of a local or national shortline holding company. This model would be representative of a potential WATCO operation as proposed by UP, or of many of the potential respondents to an RFP process initiated by the RTC. Basic assumptions included:
 - a. Shortline would share resources (management assets, equipment assets, back-office assistance, etc...) with other holding company railroads in the same region.
 - b. Holding company may have excess locomotive assets that could be utilized on this property, potentially minimizing start-up equipment costs.
 - c. All freight revenue accrues to shortline. All other corridor revenues accrue to RTC.
 - d. Full bridge and track maintenance was begun on Year 1.
2. Stand-alone and self-contained shortline railroad start-up by a private entity. Basic assumptions included:
 - a. Shortline would not share resources (management assets, equipment assets, back-office assistance) with any other entity and would fully staff for these functions.
 - b. Shortline would acquire, through purchase, locomotive assets required for operations in the corridor.
 - c. All freight revenue accrues to shortline. All other corridor revenues accrue to RTC.
 - d. Full bridge and track maintenance was begun on Year 1.
3. Shortline railroad start-up by an entity created by the RTC. Basic assumptions included:
 - a. Shortline would be a separate stand-alone entity from the RTC, but would contract with RTC for legal and financial requirements.
 - b. Shortline would acquire, through purchase, locomotive assets required for operations in the corridor.
 - c. Shortline would manage all freight operations, property management functions, project management functions and all other necessary functions in the corridor.
 - d. Shortline would carry all Railroad Liability, Property and Casualty insurance.
 - e. Shortline would be entitled to all revenues (freight, property, ancillary) derived in the corridor.³
 - f. Shortline would benefit from lower cost-of-capital than private operators.

Each scenario was modeled on a 5-year forward looking basis using customer traffic information; corridor-specific information related to track and bridge maintenance and industry accepted assumptions where specific detailed information was not available.

³ Non-freight revenues from Santa Cruz Branch Line Business Plan, August 2004 – Systra Consulting

Key to the income portion of any financial model is the projection of future carloads. As noted elsewhere in this Plan, the preponderance of traffic base on this line segment is directly tied to the activities of CEMEX at Davenport. Initial modeling was based on historic traffic levels augmented by projected future trends. Further model refinement was necessary due to recent changes in materials sourcing requirements for CEMEX which have caused a decline of inbound rail volumes of certain production inputs.

CEMEX had been receiving inbound slag material by rail and is now replacing this product with a different material. Since it is unknown at this point if this material will be transported by rail, each modeled scenario was further refined with the option of modeling current rail volumes as impacted by recent CEMEX changes, or previous rail volumes.

Year 1 pro forma Operating results for each scenario and traffic volume scenario are summarized in **Table 1** and **Table 2**.

Table 1: Year 1 Operating Summary Results – Current Rail Volumes

Santa Cruz Rail Line - Scenario Summary							
Operating Statements							
		Stand Alone - Private Company: Capitalize Equipment		SCCRTC Ownership: Capitalize Equipment		Holding Company Model	
Headcount		5		5		4	
Carloads		3,376		3,376		3,376	
Total Revenue Units		3,376		3,376		3,376	
Revenue:							
Linehaul Revenue - Carloads		\$ 1,079,350		\$ 1,079,350		\$ 1,079,350	
Non-Linehaul Revenue		-		125,000		-	
Total Revenues		\$ 1,079,350		\$ 1,204,350		\$ 1,079,350	
		Stand Alone - Private Company		SCCRTC Ownership		Holding Company Model	
Operating Expenses:							
Transportation	23.1%	\$ 249,832	20.7%	\$ 249,832	32.8%	\$ 353,857	
Roadway Maintenance	39.3%	\$ 423,970	35.2%	\$ 423,970	36.2%	\$ 390,220	
Equipment Maintenance	4.9%	\$ 52,500	4.4%	\$ 52,500	4.9%	\$ 52,500	
General & Administrative	26.8%	\$ 288,750	25.8%	\$ 310,794	19.7%	\$ 212,813	
Operating Expenses Before Deprec. &	94.0%	\$ 1,015,052	86.1%	\$ 1,037,096	93.5%	\$ 1,009,390	
EBITDA	6.0%	\$ 64,298	13.9%	\$ 167,255		\$ 69,961	
Interest Expense	2.6%	\$ 27,785		\$ 36,685		\$ 18,916	
Depreciation and Amortizatic	7.1%	\$ 77,000		\$ 77,000		\$ 27,000	
Total Operating Expenses	103.8%	\$ 1,119,837	95.6%	\$ 1,150,780	97.8%	\$ 1,055,305	
Net Income	-3.8%	\$ (40,487)	4.4%	\$ 53,570	2.2%	\$ 24,045	

Table 2: Year 1 Operating Summary Results – Previous Rail Volumes

Santa Cruz Rail Line - Scenario Summary							
Operating Statements							
	Stand Alone - Private Company: Capitalize Equipment		SCCRTC Ownership: Capitalize Equipment		Holding Company Model		
Headcount	5		5		4		
Carloads	3,876		3,876		3,876		
Total Revenue Units	3,876		3,876		3,876		
Revenue:							
Linehaul Revenue - Carloads	\$ 1,266,850		\$ 1,266,850		\$ 1,266,850		
Non-Linehaul Revenue	-		125,000		-		
Total Revenues	\$ 1,266,850		\$ 1,391,850		\$ 1,266,850		
	Stand Alone - Private Company		SCCRTC Ownership		Holding Company Model		
Operating Expenses:							
Transportation	22.5%	\$ 284,776	20.5%	\$ 284,776	30.7%	\$ 388,801	
Roadway Maintenance	33.5%	\$ 423,970	30.5%	\$ 423,970	30.8%	\$ 390,220	
Equipment Maintenance	4.1%	\$ 52,500	3.8%	\$ 52,500	4.1%	\$ 52,500	
General & Administrative	22.8%	\$ 288,750	22.5%	\$ 312,669	16.8%	\$ 212,813	
Operating Expenses Before Deprec. &	82.9%	\$ 1,049,996	77.2%	\$ 1,073,915	82.4%	\$ 1,044,334	
EBITDA	17.1%	\$ 216,854	22.8%	\$ 317,936		\$ 222,517	
Interest Expense	2.2%	\$ 28,135		\$ 32,794		\$ 15,912	
Depreciation and Amortizatic	6.1%	\$ 77,000		\$ 77,000		\$ 27,000	
Total Operating Expenses	91.2%	\$ 1,155,131	85.0%	\$ 1,183,709	85.8%	\$ 1,087,245	

Summary of Modeled Results

1. The intermediate (3-5 years) viability of any outside private freight railroad operation in the corridor is almost entirely dependent upon CEMEX's ability to continue to utilize rail transportation for inbound production inputs and outbound finished products.
2. The best possibility for a "viable" shortline operation is one where the shortline (privately-owned or established as an agency by the RTC) receives *all* revenues from the corridor (freight, leases, easements, ancillary, etc...), and where the RTC is ensured that all revenues are invested in the shortline operation. This added income helps to minimize downside risks associated with changes in traffic volumes at CEMEX, and, in the case of an outside private operator, could provide for a more favorable capitalization structure.
3. Significant changes in CEMEX's use of rail...positively or negatively...almost completely flow to bottom line EBITDA, Net Income and Cash Flow.
4. Long-term viability (beyond 7-10 years) of any outside private freight railroad operation in the corridor beyond Watsonville will continue to be dependent upon CEMEX's use of rail.

5. Track and structures maintenance expenses exceed that of typical shortline railroads of this size, operating mileage and traffic base. This is due to the topography through which the railroad operates and the number of bridge structures in the rail corridor.

*Full discussion of Financial Analysis and modeling work, including assumptions and full five year analysis is contained in **Section 4: New Shortline Railroad Operations - Financial Analysis of Shortline Operations.***

Summary of Research Results

1. Ability to recapture lost CEMEX inbound rail traffic will be a function of sourcing locations for CEMEX, rail rates provided by UP, and equipment availability suitable for movement of new product.
2. Ability to expand CEMEX's use of rail for outbound shipments will be a function of obtaining competitive rail rates to additional destination locations and working with UP to modify certain local operating practices to make rail more competitive in current destination locations.
3. Ability for Lumberman's to receive inbound lumber by rail is important in their ability to remain competitive in the marketplace. Their competitors throughout the region receive lumber product via rail.
4. Potential opportunities may exist to develop freight rail traffic in partnership with the City of Santa Cruz Public Works Department.
5. Potential opportunities may exist to develop additional outbound freight rail traffic on behalf of CEMEX.
6. Long-term opportunities exist to develop additional freight rail volumes in Watsonville to support the produce industry in the region. Developing these opportunities will require focused, pro-active work by the shortline with local Watsonville industry and the UP.
7. Long term opportunities may exist to develop other freight rail volumes in the Watsonville to support non-agricultural industry in the region.

*Full discussion of additional opportunities, including requirements, barriers and constraints and related assumptions is contained in **Section 4: New Shortline Railroad Operations – Marketing / Business Development Plan.***

Notes

Section 2

Analysis of Current Operations

Local Railroad Service – Watsonville to Davenport

Local rail service from Watsonville to Davenport is provided by the UP's "**Santa Cruz Local**" four (4) days per week, occurring on Monday, Tuesday, Wednesday and Friday. Service occurs generally during daylight hours, with the outbound train departing Watsonville mid-morning and returning to Watsonville late afternoon.⁴

The Santa Cruz Local currently does not provide service to customers in Watsonville. Rail customers in Watsonville are served by other local and switching operations conducted out of Watsonville Yard⁵. Upon a sale of the corridor to RTC, it is assumed that the **UP** will no longer serve the Watsonville customers in the corridor and they will be served by the shortline railroad operating in the corridor.

Local rail service from Santa Cruz to customers in Felton is provided by the **Santa Cruz, Big Trees and Pacific Railway ("BT&P")**.



Santa Cruz Rail Corridor encompasses 32 miles from Watsonville Jct. to Davenport

⁴ Interview with CEMEX, 10/3/2008 confirmed by UP management 10/4/2008

⁵ UP Roadmaster DeWayne Hillman 10/4/2008

Primary workload of the Santa Cruz Local includes:

- Service as required to Lumberman's facility in Soquel
- Interchange traffic with the **BT&P** at Santa Cruz for furtherance to Felton
- Service to CEMEX in Davenport for inbound raw materials and outbound finished cement

Operational Considerations

Operating Restrictions

UP has the following operating restrictions in the Watsonville – Davenport rail corridor:⁶

- Track Speed is limited to 10 mph
- Train Tonnage (excluding locomotives) is limited to 3000 tons
- Trailing Length of Train (excluding locomotives) is limited to 2000 feet
- Maximum weight per car is 268,000 pounds

These operating restrictions have been adopted by the **UP** due to ruling grades and curvature of the mainline and the carrying capacity of the bridge structures.



Ruling grade, track curvature and carrying capacity of the majority of bridge structures have required the UP to adopt specific operating restrictions in the Watsonville – Davenport rail corridor

⁶ UP Roseville Area Timetable No. 4 dated 12/18/2005

Street Running and Interaction with Public Venues

The Watsonville – Davenport rail corridor is characterized by significant areas of “street running” where the mainline bisects high-density street thoroughfares. The two primary areas of street running are:

- Walker Street in Watsonville
- Beach Street in Santa Cruz



Street running in Watsonville includes an approximately $\frac{3}{4}$ mile section along Walker Street



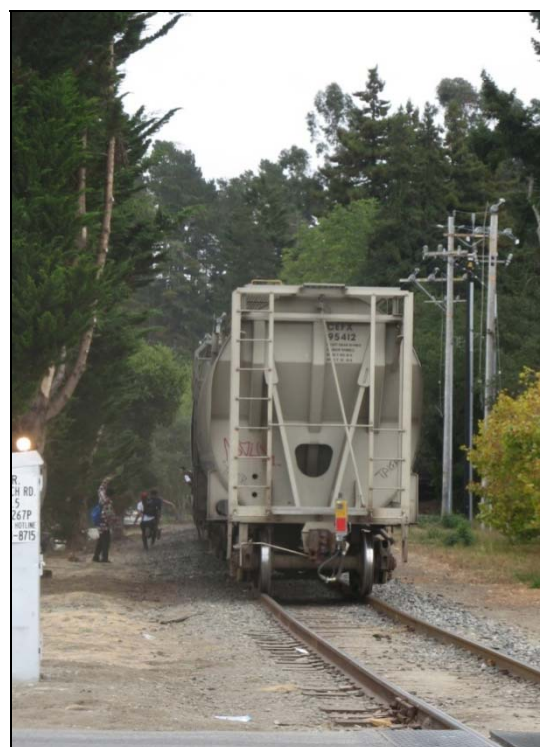
Street running in Santa Cruz along Beach Street demonstrates the close interaction between rail operations and vehicular / pedestrian traffic

In addition to areas of street running, the Watsonville – Davenport rail corridor is characterized by several areas of close interaction with high-density public venues, including:

- Santa Cruz Beach Boardwalk
- Aptos



Santa Cruz Beach Boardwalk



Aptos (note "hitchhikers" riding and chasing train)

Maintenance Considerations

The topography through which the rail line traverses creates special rail line maintenance considerations with respect to the following.

- Bridge Maintenance
- Drainage
- Vegetation Control

Bridge Maintenance

32 bridges and 9 major culverts are located in the Watsonville – Davenport rail corridor. While specific details of UP's bridge maintenance program are not available, independent work done by engineers contracted by the RTC indicate that significant and ongoing expenditures are necessary to maintain bridge structures to their current state of repair and carrying capacity.



Rail bridge at Capitola is one of 32 rail bridges in the Watsonville – Davenport rail corridor

Drainage and Vegetation Control

Sections of rail line between Watsonville and Aptos and between Santa Cruz and Davenport require particular attention with respect to drainage, and the control of invasive weeds and other vegetation.



Heavy vegetation between Watsonville and Aptos; and the proximity to farm fields and beaches north of Santa Cruz require frequent attention to insure the right-of-way is not fouled with weeds, mud and sand

Notes

Section 3

Transaction Options for New Shortline Railroad Operations

Union Pacific Proposed Option

Overview

The UP has discussed a transaction structure related to their sale of the Watsonville – Davenport rail line corridor and the establishment of shortline railroad operations in the corridor. This structure is modeled around what UP considers a similar transaction which occurred in 2002 and 2007 between the UP and the Utah Transit Authority (UTA).

In the UTA transaction, UP sold railroad right-of-way assets to the local transportation agency for use in commuter rail operations.⁷ Separately, UP selected a shortline railroad operator to conduct freight rail operations in the corridor.

A review of the documents related to the UTA transaction and using the UTA transaction as a proxy indicates that the proposed UP transaction with the RTC will have a number of the following elements:

Commercial and Operational

1. UP would reserve a freight rail easement from the sale of the corridor to the RTC. Either prior to, or concurrent with the close of escrow, the UP shall select the shortline railroad operating company that will serve the freight rail customers in the corridor and to this operator, convey the reserved easement together with the Common Carrier responsibility.

Under this arrangement, UP would negotiate with, and maintain exclusive access with the shortline operator on such items as:

- a. All commercial agreements related to the handling of freight traffic and service to local customers;
- b. All issues related to car supply, car hire and demurrage;
- c. All revenue allowances to be paid to the shortline for handling freight traffic;
- d. Any lease, trackage rights or additional operating agreements required by the shortline to create operational efficiencies beyond the acquired corridor;
- e. Railroad Legal Liability insurance requirements.

⁷ STB Finance Docket No.'s 34170 and 35008 – Utah Transit Authority – Acquisition Exemption–Certain Assets of Union Pacific Railroad Company, January 28, 2002 and July 20, 2007.

2. It is unclear at this point whether UP would be involved in any of the negotiations between the RTC and the shortline operator on non-freight railroad issues involving use of the corridor. An **Administration and Coordination Agreement** with the shortline operator would need to be developed to address these uses and include items such as:
 - a. Track and bridge maintenance requirements imposed by RTC;
 - b. Any specific liability insurance requirements of the RTC;
 - c. Specific service expectations of the RTC;
 - d. Expectations related to additional future use of the corridor for:
 - i. Tourist rail operations
 - ii. Commuter rail operations
 - iii. Mixed-use “rails and trails”

Legal

Legal elements related to this potential transaction structure have been outlined in a separate Memo by prepared by Kirk Trost, Attorney with Miller, Owen and Trost.

UP’s Choice of Shortline Operator

The UP has indicated that it is their preference, and potentially their *requirement* that WATCO Companies, Inc., based out of Pittsburg, Kansas establish and operate the shortline railroad in the Watsonville – Davenport corridor as part of the proposed transaction with the RTC.

WATCO has a long history of completing shortline transactions with the UP. Several WATCO shortline railroad properties are former UP rail line segments throughout the Midwest and Western US.

WATCO Background

WATCO Companies, Inc. was started in 1983 by Charles R. "Dick" Webb. Their first operation was an industrial switching operation in DeRidder, Louisiana that is still in existence today. From that small beginning, WATCO has grown to become a diversified holding company with interests in shortline and regional railroad operations and rail-related value added service and equipment companies.

The company remains privately held by the Webb family, who are also active in the day-to-day management of the organization.

WATCO’s holdings include:

- 18 shortline / regional railroads operating in 15 different states;
- Industrial and contract switching services;
- Locomotive and rail car repair and leasing services;
- Transloading and warehousing services

WATCO Company Structure⁸

WATCO is headquartered in Pittsburg, KS where the majority of management and back-office personnel are based. WATCO does maintain a regional management structure as well, with their Western Region headquarters being located in Twin Fall, Idaho with oversight responsibility for the states of Oregon, Washington, Idaho, Montana and North Dakota.

WATCO's California operations currently consist of a couple of industrial switching operations and the newly-formed "Pacific Sun Railroad, LLC" which operates between San Diego and the Orange County border in southern California.

Of WATCO's 18 railroad operations:

- 11 are operated under Lease Agreement with a Class 1 railroad;
- 5 are owned outright by WATCO;
- 2 are operated under a Freight Easement arrangement on current or future commuter railroad operations (Austin Western RR in Austin, TX; Pacific Sun Railroad, LLC.)

RTC Role

Capital Requirements

The RTC would provide capital under the UP-Proposed Transaction Structure for the following:

- \$14.2 million for acquisition of right-of-way corridor from Watsonville Jct. to Davenport.
- \$5.0 million (approximate) for necessary capital improvements to Bridges and Track Structure in the corridor.

Management, Administrative and Insurance Requirements

Oversight management and administration requirements of the RTC under the initial UP-proposed option appear to be the least burdensome of all Option Scenarios. This is due primarily to the UP selecting their own shortline operator, and entering into all necessary commercial agreements with the operator and managing all commercial aspects of the relationship.

Anticipated responsibilities for the RTC under the UP proposal include:

- Administration and oversight of the planned \$5 million Capital Projects investment in corridor;
- Property management and administration;
- Oversight of *Administration and Coordination Agreement* with Shortline on
 - Auditing maintenance standards
 - Auditing required performance or service metrics.

⁸ WATCO Companies website, 11/28/2008.

- Monthly reports to RTC on railroad status

These functions can potentially be absorbed by current RTC Staff or can be contracted to an outside management entity. It is estimated that these functions would carry the necessary personnel burden of no more than ½ Full Time Equivalency.

As with all of the Option Scenarios discussed, when other non-freight uses of the corridor are developed (passenger tourist and commuter rail operations), additional management and administrative responsibilities will be required with an attendant increase in cost.

The RTC will likely secure Property and Casualty Insurance to cover the loss of major structures in the corridor. The RTC may also need to secure Liability Insurance coverage for non-freight-railroad related incidents which may occur on the property.

Revenue Opportunities for RTC

Revenues would accrue to the RTC primarily through existing leases, easements, and occupancy permits from uses and occupancies in the corridor. The amount of such revenue now going to UP, and the status of these occupancies is not now known.

One conservative estimate of the revenue stream, based on a comparison with Monterey Branch revenue accruing to the Transportation Agency for Monterey County (TAMC), is \$170,000 per year.⁹

Current uses that may be generating revenue as well as future considerations include:

- Making the corridor available for uses by utilities;
- Ensuring that all agreements have been updated with appropriate inflation escalators;
- Selling excess property for other uses and community benefit;
- Making the corridor and structures available for advertising opportunities, if appropriate.

⁹ Santa Cruz Branch Line Business Plan, August 2004 – Systra Consulting.

The following Table summarizes Revenue opportunities, Expense requirements and Capital obligations for RTC under the UP-Proposed Transaction Structure.

<u>Revenue Opportunities</u>	Available to RTC	\$ Amount (low)	\$ Amount (high)
<i>Direct Freight Income</i>	No	0	0
<i>Revenue Share of Freight Income</i>	No	0	0
<i>Lease, Easement and Occupancy Income</i>	Yes	\$125,000	\$170,000 ¹⁰
<i>Ancillary Income (advertising, etc...)</i>	Yes	Unknown	unknown
Total Revenues Range		\$125,000	\$170,000
<u>Expense Requirements</u>	Required of RTC	\$ Amount (low)	\$ Amount (high)
<i>Railroad Administration</i>	Yes	\$35,000	\$50,000 ¹¹
<i>Property and Casualty Insurance</i>	Yes	\$45,000	\$65,000
<i>Liability Insurance</i>	Maybe	\$10,000	\$15,000
Total Expenses Range		\$90,000	\$130,000
<u>Capitalization Requirements</u>			
<i>Rail Line Acquisition Capital</i>	Yes	\$14.2 million	\$14.2 million
<i>Capital Projects</i>	Yes	\$5.0 million	\$5.0 million
<i>Start-Up Capital for Operations</i>	No	0	0
<i>Start-Up Capital for Equipment Acquisitions</i>	No	0	0
Total Capitalization Requirements		\$19.2 million	\$19.2 million

¹⁰ Santa Cruz Branch Line Business Plan, August 2004 – Systra Consulting.

¹¹ Assumes ½ Full Time Equivalent position or management fee.

RTC Option – RFP for Shortline Operator

Overview

The RTC has contemplated a transaction structure whereby it would issue an RFP to hire a shortline railroad operator to provide freight rail service as opposed to accepting the selection made by the UP.

This transaction differs fundamentally from the UP-Proposed Transaction Structure in that it closely ties all of the activities of the shortline railroad with the interests of the RTC. It creates the primary relationship between the shortline and the RTC whereas the UP-Proposed Transaction Structure significantly distances the shortline from the RTC regarding nearly all commercial activity conducted in the corridor.

For these reasons and likely others yet to be discovered, the RFP Option is not a transaction structure currently supported by the UP. If, however, this were the eventual structure for establishing a shortline in the corridor, it would likely contain the following elements:

Commercial and Operational

1. The RTC would acquire the corridor intact with all commercial and operating rights that would go along with ownership of an intact and assembled rail corridor. UP would not retain any freight easements in the corridor.
2. The RTC would either:
 - Create a Freight Rail Easement in the corridor and prior to, or concurrent with the close of escrow, select the shortline railroad operating company that will serve the freight rail customers in the corridor and to this operator, convey the easement together with the Common Carrier responsibility, for a Term or successive Terms, or;
 - Create an Operating Lease contract with the shortline railroad operating company selected to provide service to freight rail customers in the corridor, for a Term or successive Terms.
- a. Either the Easement Conveyance or the Operating Lease Contract would need to include provisions to address such issues as:
 - i. Any payment structures from the shortline to the RTC for granting freight easement or as payment on lease;
 - ii. Track and bridge maintenance requirements imposed by RTC;
 - iii. Any specific liability insurance requirements of the RTC;
 - iv. Specific service expectations of the RTC;
 - v. Expectations related to future non-freight use of the corridor.

3. The shortline would likely become a “Handling Carrier” for UP in the corridor and negotiate with them on such items as:
 - All commercial agreements related to the handling of freight traffic and service to local customers;
 - All issues related to car supply, car hire and demurrage;
 - Revenue allowances to be paid to the shortline for handling freight traffic;
 - Any lease, trackage rights or additional operating agreements required by the shortline to create operational efficiencies beyond the acquired corridor;
 - Railroad Legal Liability insurance requirements if shortline operated on UP-owned track (i.e.: Watsonville Yard).

Legal

Legal elements related to this potential transaction structure have been outlined in a separate Memo by prepared by Kirk Trost, Attorney with Miller, Owen and Trost.

RTC Role

Capital Requirements

The RTC will provide capital under the RFP- Option Transaction Structure for the following:

- \$14.2 million for acquisition of right-of-way corridor from Watsonville Jct. to Davenport.
- \$5.0 million (approximate) for necessary capital improvements to Bridges and Track Structure in the corridor.

Management, Administrative and Insurance Requirements

This proposal is built upon the assumption that the resulting relationship between the shortline and the RTC will be a “hand-in-glove” partnership arrangement with both parties working for the mutual benefit of each other and the region.

Oversight management and administration requirements of the RTC under this option would likely increase given the primary nature of the relationship between the shortline and the RTC and what would hoped to be a close working relationship designed to grow the vitality of rail operations in the corridor.

Anticipated responsibilities for the RTC under this proposal include:

- Administration of shortline RFP process;
- Administration and oversight of the planned \$5 million Capital Projects investment in corridor;
- Property management and administration;

- Working with shortline, current customers, communities and development stakeholders on opportunities to enhance the railroad's utility in the corridor;
- Work with shortline on non-freight revenue opportunities for corridor (tourist rail, etc...);
- Oversight of Lease and Operating Agreement with Shortline;
- Monthly reports to RTC on status of railroad.

It is estimated that these functions could carry the personnel burden of up to 1 Full Time Equivalent position. These functions can either be managed in-house by the RTC or contracted to a management company.

As with all of the Option Scenarios discussed, when other non-freight uses of the corridor are developed (passenger tourist and commuter rail operations), additional management and administrative responsibilities will be required with an attendant increase in cost.

Revenue Opportunities for RTC

In addition to Revenue Opportunities already identified, the RTC may elect to create a "gain-sharing" revenue mechanism that provides a growing revenue stream to the RTC based upon growth in carloads above certain threshold amounts.

Given the marginal economics of the freight-only rail operation based upon current traffic volumes, realistic expectations and thresholds would need to be established with the shortline operator for any gain-sharing revenue opportunity.

The following Table summarizes Revenue opportunities, Expense requirements and Capital obligations for RTC under the RFP-Option Transaction Structure.

<u>Revenue Opportunities</u>	Available to RTC	\$ Amount (low)	\$ Amount (high)
<i>Direct Freight Income</i>	No	0	0
<i>Revenue Share of Freight Income</i>	Maybe	0	0
<i>Lease, Easement and Occupancy Income</i>	Yes	\$125,000	\$170,000 ¹²
<i>Ancillary Income (advertising, etc...)</i>	Yes	Unknown	unknown
Total Revenues Range		\$125,000	\$170,000
<u>Expense Requirements</u>	Required of RTC	\$ Amount (low)	\$ Amount (high)
<i>Railroad Administration</i>	Yes	\$75,000	\$95,000 ¹³
<i>Property and Casualty Insurance</i>	Yes	\$45,000	\$65,000
<i>Liability Insurance</i>	Maybe	\$10,000	\$15,000
Total Expenses Range		\$130,000	\$175,000
<u>Capitalization Requirements</u>			
<i>Rail Line Acquisition Capital</i>	Yes	\$14.2 million	\$14.2 million
<i>Capital Projects</i>	Yes	\$5.0 million	\$5.0 million
<i>Start-Up Capital for Operations</i>	No	0	0
<i>Start-Up Capital for Equipment Acquisitions</i>	No	0	0
Total Capitalization Requirements		\$19.2 million	\$19.2 million

¹² Santa Cruz Branch Line Business Plan, August 2004 – Systra Consulting.

¹³ Assumes 1 Full Time Equivalent position or management fee.

RTC Option – RTC Creation of Shortline

Overview

The RTC may elect to create an entity to own and operate the shortline railroad operating in the Watsonville – Davenport corridor.

This type of transaction and operational structure could be established in one of the following fashions:

1. A separate operating entity would be created by the RTC and installed as the designated operator of RTC-owned assets. This entity would enter into a similar type of Lease and Operating Agreement with the RTC that an outside shortline would enter, detailing rights, responsibilities and revenue-sharing arrangements.
2. A separate operating entity would be created by the RTC and installed as the designated operator and manager of RTC-owned assets. This entity would oversee all aspects of the corridor, including:
 - Freight operations;
 - Lease, easement and occupancy administration;
 - Capital projects management;
 - Management or oversight of potential tourist passenger operations;
 - Management or oversight of potential commuter rail passenger operations;
 - Management, coordination and oversight of potential trail development in the corridor.

This entity would be entitled to all revenues derived from freight operations and property management.

This operating entity would likely become a “Handling Carrier” for UP in the corridor and establish agreements to govern such issues as:

- All commercial aspects related to the handling of freight traffic and service to local customers;
- All issues related to car supply, car hire and demurrage;
- Revenue allowances to be paid to the shortline for handling freight traffic;
- Any lease, trackage rights or additional operating agreements required by the shortline to create operational efficiencies beyond the acquired corridor;
- Railroad Legal Liability insurance requirements if shortline operated on UP-owned track (i.e.: Watsonville Yard).

It is not known at this time whether UP would be supportive of this type of transactional structure for sale of the corridor and establishment of shortline operations.

Several successful examples of public-owned, for-profit shortline railroad operations exist in North America, including:

<i>Alaska Railroad</i>	Owned by State of Alaska
<i>Canton Railroad Company</i>	Owned by State of Maryland (serves Port of Baltimore)
<i>Columbia Terminal Railroad</i>	Owned by City of Columbia, MO
<i>South Carolina Public Railways</i>	Owned by SC Department of Commerce
<i>Tacoma Municipal Belt</i>	Owned by Tacoma Public Utilities

Advantages of RTC Ownership

Potential advantages may exist for a unit of government or unit of the RTC to own and operate the shortline railroad in the corridor, including:

- Potentially aligns all of the interests in the region for the use and development of the corridor under the auspices of RTC;
- Streamlines transaction time with UP as it removes the need for separate document development and subsequent negotiations with WATCO;
- Provides complete control and coordination efficiency for the RTC over all activities in the corridor;
- Minimizes duplication of management efforts as railroad GM would also perform administrative responsibilities required under other transaction options;
- Could minimize or eliminate duplicate or overlapping insurance coverage as shortline would carry all necessary Liability, Property and Casualty insurance coverage;

Disadvantages of RTC Ownership

Several potential disadvantages may exist for a unit of the RTC to own and operate the shortline railroad in the corridor, including:

- Normal business risk associated with operating any for-profit business;
- Thin current margins of railroad;
- Common Carrier responsibility;
- Any catastrophic loss to right-of-way or structures will be fully borne by RTC / operating entity. Losses exceeding insurance coverage will require securing additional capital;
- Finding, hiring and training qualified railroad operating professionals and management

The following Table summarizes Revenue opportunities, Expense requirements and Capital obligations for RTC under the RTC establishment of Shortline operations.

<u>Revenue Opportunities</u>	Available to RTC	\$ Amount (low)	\$ Amount (high)
<i>Direct Freight Income</i>	Yes		0
<i>Revenue Share of Freight Income</i>	Maybe	0	0
<i>Lease, Easement and Occupancy Income</i>	Yes	\$125,000	\$170,000 ¹⁴
<i>Ancillary Income (advertising, etc...)</i>	Yes	Unknown	unknown
Total Revenues Range		\$125,000	\$170,000
<u>Expense Requirements</u>	Required of RTC	\$ Amount (low)	\$ Amount (high)
<i>SCCRTC Railroad Administration</i>	Yes	\$15,000	\$25,000
<i>Property and Casualty Insurance</i>	Maybe	\$10,000	\$15,000
<i>Liability Insurance</i>	Maybe	\$10,000	\$15,000
Total Expenses Range		\$35,000	\$55,000¹⁵
<u>Capitalization Requirements</u>			
<i>Rail Line Acquisition Capital</i>	Yes	\$14.2 million	\$14.2 million
<i>Capital Projects</i>	Yes	\$5.0 million	\$5.0 million
<i>Start-Up Capital for Operations</i>	Yes	\$150,000	\$180,000 ¹⁶
<i>Start-Up Capital for Equipment Acquisitions</i>	Yes	\$90,000	\$850,000 ¹⁷
Total Capitalization Requirements		\$19.44 million	\$20.23 million

¹⁴ Santa Cruz Branch Line Business Plan, August 2004 – Systra Consulting

¹⁵ Majority of expenses are fully absorbed by shortline railroad.

¹⁶ Covers Start-up Expenses and 90 days of Working Capital.

¹⁷ Range is dependant upon whether locomotives are purchased or secured through Operating Lease.

Notes

Section 4

New Shortline Railroad Operations

Operating Plan

The final Operating Plan for the Watsonville – Davenport rail line corridor will be determined based on a variety of variables, including:

- Carload volumes
- Changes in customer service requirements
- Changes in interchange frequency or requirements with UP in Watsonville

For modeling and analysis purposes, a standardized Operating Plan was developed based upon a stand-alone, self-sufficient operation serving a variable level of carload volumes.

Staffing for Operations

Basic staffing for an operation of this size would be as follows:

- (1) General Operations Manager, with the following responsibilities:
 1. Oversight management of all rail operations;
 2. Oversight management of Maintenance of Way;
 3. Qualified as locomotive engineer to fill in as relief on vacation days, sick days and as other needs require.
 4. Management of marketing / business development initiatives of the railroad.
- (2) Full time Train Service employees responsible for daily train operations. Crews shall be cross-trained to perform minor track maintenance duties as required.
- (1) Full time Roadmaster to administer all aspects of track and bridge maintenance, perform minor maintenance as required and oversee track and bridge maintenance subcontractors.
- (1) Full time Track Maintenance Laborer / Signal Maintainer responsible for working with Roadmaster on minor track maintenance items, including: spot tie replacement, grade crossing maintenance, and other track maintenance requirements and responsible for minor maintenance and upkeep of signalized grade crossings and other signals controlling operations in the corridor.

Contracted Services

The following services are anticipated to be contracted:

1. “Production” Maintenance of Way, including:
 - a. Tie Replacement;
 - b. Ditching and drainage;
 - c. Ballast replacement and surfacing;
 - d. Weed Spraying;
 - e. Bridge maintenance and repair;
 - f. Signal maintenance and repair
2. Locomotive Inspections, Maintenance and Repair

Daily Operating Plan

Frequency of Service

Service frequency will be entirely dependent upon carload volumes. Based on current carload volumes, cost-effective service can be provided to all customers on a 3-day / week basis. If carload volumes return to previous levels, (i.e., a return of inbound CEMEX traffic) service levels could be returned to a 4-day / week basis.

Basic Service Schedule

The following would be a reasonable service plan for a railroad operating in the Watsonville – Davenport rail corridor. The service plan assumes that arrangements can be made to store the locomotives overnight on property at or adjacent to Union Pacific’s yard in Watsonville:

Davenport Turn: On duty at 6:00 am at Watsonville

- | | |
|---|--------------------|
| ➤ Switches local Watsonville industry: | 6:30 – 8:00 am |
| ➤ Interchanges cars in Santa Cruz for BT&P : | 10:00 – 10:30 am |
| ➤ Services CEMEX facility in Davenport: | 11:15 – 12:00 noon |
| ➤ Services Lumberman’s Soquel facility (if needed): | 1:15 – 1:30 pm |
| ➤ Additional switching in Watsonville (if needed): | 2:30 – 4:00 pm |

This Service Schedule would be followed under a 3 or 4-day / week operating frequency. Not all customers will require service on all operating days.

Weekend and Holiday Service will be provided to customers at a premium rate as needed.

Other Operating Considerations include:

- The General Code of Operating Rules (GCOR) will be applied to operations. This is consistent with current UP practice. The line will continue to be operated as an “Industrial Lead – Other Than Main Track”.
- If designated “Industrial Lead – Other Than Main Track”, the maximum authorized speed on the line would be 20 mph. The line segment between Santa Cruz and Davenport appears to have the capability of handling this track speed. From Santa Cruz to Watsonville, track speed would likely be limited to 10 mph due to gradient, curvature and numerous bridge structures.

Interchange Requirements with UP

Specific changes in operating practices will need to be implemented by the UP to allow for efficient operation of a shortline between Watsonville to Davenport, including:

1. Yard Space allocation in Watsonville Yard:
 - a. The current UP Santa Cruz Local does not serve local Watsonville industry. As understood by this consultant team, the UP outsourcing plans call for the new shortline to provide local service in Watsonville. Inclusion of such Watsonville customers helps to increase the traffic base to an acceptable threshold. The inclusion of the Watsonville local traffic would require a shortline to have direct access to a sufficient number of yard tracks in Watsonville Yard in order to build their train “in station order” (to place a train in station order is to arrange the cars in proper sequence in the train to effect the most efficient handling of cars en route) prior to departing Watsonville Yard. Tracks required would include:
 - i. Inbound Receiving Track
 - ii. Outbound Departure Track
 - iii. 1 or 2 “working” tracks to make up train in station order
 - iv. A “Run-around” track to allow train crew to work both ends of their train
 - v. Storage tracks as required by CEMEX for empty cement hoppers and loaded coal / iron ore cars.
2. Pre-negotiated agreement on administration and management of car-hire expenses. Car-hire is the daily cost for railroad-supplied equipment used in the transportation of commodities. This mechanism could fall under two basic scenarios:
 - a. Apply industry standards which allow a certain number of “free-days” for non-private railroad equipment on line; or,
 - b. UP and shortline could agree to a set rate for non-private railroad equipment to cover the cost of carhire for up to 4 days while railroad cars are on the shortline.

Initial Equipment Requirements

Locomotives

A minimum of 2 locomotives will be required to provide freight service in the corridor based on current traffic volumes. Carload volumes and the resulting economics will dictate whether additional locomotives units are required.

Locomotives used in the corridor have been generally restricted to “4-axle” units, that is, locomotive units with two powered axles per truck. This restriction is due to degree of curvature in some locations in the corridor.¹⁸

Options for an independent or RTC-owned shortline for use in the corridor would include:

1. “GP38-2” – type locomotives:

- a. Follows current UP operating practices
- b. Units are readily available for purchase or lease
 - i. Purchase Price: \$325,000 - \$375,000 / unit
 - ii. Lease Rate: \$165 - \$185 per day / unit



The GP38-2 locomotive is a standard locomotive type used by many shortlines and currently used by UP in the Watsonville – Davenport corridor.

¹⁸ UP Roseville Area Timetable No. 4 dated 12/18/2005

2. “SW1500” – type locomotives:

- a. Better overall visibility of surroundings for operating personnel than GP38-2
- b. Slightly better fuel economy than GP38-2 but 25% lower horsepower than GP38-2
- c. Units are generally available for purchase or lease

- i. Purchase Price: \$275,000 - \$350,000 / unit
- ii. Lease Rates: \$125 - \$145 per day / unit



The SW1500 locomotive would be an appropriate locomotive choice for the Watsonville – Davenport corridor given the excellent visibility it provides for train crews.

3. “Mother-Slug” –type locomotive consist:

- a. More specialized locomotive arrangement, with prime mover (engine) providing power to traction motors in two units
- b. Greater fuel efficiency and maintenance costs than two fully-powered units
- c. Units will need to be special-ordered, but can be purchased or leased
 - i. Purchase Price: \$650,000 - \$700,000 for two-unit consist
 - ii. Lease Rate: \$300 - \$350 per day / two-unit consist



A “Mother-Slug” locomotive consist would provide fuel and maintenance savings over two fully powered locomotive units. This type of consist is widely used on shortline and switching railroads.

Marketing / Business Development Plan

Development Strategy

The shortline operating in the Watsonville – Davenport corridor should develop a multi-faceted marketing and business development strategy designed around the following strategic objectives:

- Maximizing the rail volumes from the current customer base
- Attracting former rail-served customers to utilize rail
- Identifying new potential rail-served customers in the region
- Working with local development entities to attract new rail-served business to the region

This strategy, long-term could diversify the customer base and commodity mix, which is especially important given the current concentration of rail traffic.

The following section highlights specific new or expanded business opportunities in the corridor that have been identified by the consulting team.

Carload Opportunities - CEMEX

Inbound Production Inputs

CEMEX recently eliminated a slag material from their production inputs. This product was received into CEMEX by rail and has had the effect of reducing rail volumes by over 500 rail cars per year. This reduction has been built into current financial modeling of shortline rail operations.

CEMEX has explored replacing this slag material with an iron ore product. Discussions with CEMEX indicate that 2 of the potential 3 sourcing locations of this material would provide favorable economics to transport this material by rail. CEMEX has indicated that fewer rail cars of this material would be required given its density compared to the formerly-used slag material.

Volume Potential

- Specific volume potential hasn't been fully quantified, but it can be reasonably inferred that if CEMEX was able to utilize rail for this product, it would restore 400 – 450 annual carloads per year to the operation.

Keys to Success

- CEMEX must choose a rail-served origination location for sourcing this new material
- UP must provide competitive rail transportation rates to move this material vs. current trucking options
- UP must be willing to provide appropriate rail equipment necessary to move the product

Outbound Cement

Current economic conditions have caused a significant drop in the demand for cement. As economic conditions improve, outbound volumes should improve as well.

In addition to current rail-served options for outbound cement, additional opportunities may exist to expand into markets currently served by truck. Key among these markets is the CEMEX cement terminal located at the Port of Redwood City. This terminal is currently predominantly truck-served from Davenport.

Volume Potential

- CEMEX has indicated that up to 50,000 tons per year of cement could be transferred to rail given favorable economics. This translates into 450 – 475 new annual carloads.

Keys to Success

- UP needs to modify their current operational practices between Watsonville – San Jose – Roseville (Sacramento) to allow for the drop-off of CEMEX cars in San Jose for furtherance to Redwood City. Current UP operational practices do not allow for this, and cars are moved to Roseville before returning to Bay Area. This adds transportation cost and delays.
- UP needs to provide a “10-car” unit-train rate to CEMEX for cars terminating in Redwood City in addition to providing a different operational scheme.

Inbound Aggregate Material

CEMEX has indicated that if a different service rail service package between Port of Redwood City and Davenport could be established, additional opportunities to bring in aggregate materials by rail could develop.

Volume Potential

- Specific volumes potentials have not been identified

Keys to Success

- UP must be willing to adopt and fairly-price a different operational practice in order to attract this traffic.

Carload Opportunities – City of Santa Cruz Public Works Department

Inbound Ferric Chloride

The City of Santa Cruz Public Works Department utilizes Ferric Chloride as a wastewater treatment medium. Ferric Chloride causes material in the waste stream to precipitate out as a sludge, which is then captured by mechanical and filtering means.

Currently, ferric chloride is delivered to Public Works by truck. It is commonly delivered by rail throughout the country from manufacturing locations.

Volume Potential

- Specific volume potentials have not yet been identified, but other communities of similar size to Santa Cruz would typically utilize the equivalent of 20 – 30 rail cars per year. In addition to Santa Cruz, other communities in the region could also bring this product in by rail, adding an additional 40 – 60 carloads. This commodity is higher-value in nature and could command a higher per-car revenue allowance to the shortline railroad.

Keys to Success

- Securing a truck-competitive rail rate from UP to make rail delivery attractive.
- Necessary track and unloading infrastructure at water treatment plant to make direct delivery possible.

Outbound Waste Sludge

Public Works is evaluating the potential of shipping processed waste sludge from wastewater stream to CEMEX for use as a fuel additive in their kiln.

Volume Potential

- Annual tonnage potential is approximately 12,000 – 14,000 tons. This equates to 130 – 150 annual rail car movements. Especially attractive of this potential is that it is entirely self-contained in the corridor and does not require any involvement by UP.

Keys to Success

- Testing of material at CEMEX needs to be successful.
- Necessary infrastructure for loading / unloading railcars needs to be established.
- Appropriate rail car equipment to move product needs to be identified and secured.

Carload Opportunities – Watsonville Area

Inbound Agricultural Inputs

Studies and initiatives are being pursued by the *Growers – Shippers Association of Central California* to utilize rail to a greater extent for the benefit of its constituency base. This group represents the majority of agricultural interests in southern Santa Cruz County, Monterey County and Salinas County.

General opportunities exist to develop a centralized “depot” to coordinate the inbound movement of agricultural inputs such as pesticides, herbicides and fertilizers. This depot could potentially serve the agricultural base in Santa Cruz, Monterey and Salinas Counties. It is likely these materials are currently being transported by rail to a Bay Area destination and trucked for local delivery.

Volume Potential

- Current volume potentials by commodity are not known at this time, however, anecdotal research indicates that potential carloads volumes could range between 200 – 250 carloads per year.

Keys to Success

- Coordination of end-users to consolidate their inbound delivery from a central location.
- Establishment of transload location in Watsonville that can be permitted to handle these materials.
- Favorable rail rates from UP for movement of these products.

Outbound Agricultural Products

Significant and excess warehouse (frozen and dry) capacity exists in Watsonville. Opportunities may exist to establish new options for agricultural producers in the region to utilize rail for their outbound requirements.

Continued work with *Growers – Shippers Association* and other groups in the region will quantify the potential of these opportunities.

General Development Opportunities

Transload Facility Development

A “Transload Facility” extends the reach of the railroad by providing a centralized location to load / unload and store a variety of products for customers not directly served by rail. Other services provided by a full-service transload facility can include: warehousing, inventory management, and local trucking delivery and pick-up of products.

Watsonville appears to be the most suitable location for the future development of a rail-served transload facility.

Products typical moving through a transload facility would include:

- Steel and ductile iron pipe
- Wooden transmission poles
- Lumber and building products
- Coiled / rolled steel, wire and rebar
- Chemicals, fuels and solvents
- Plastics
- Construction materials



A large full-service rail transload facility can combine warehousing as well as outdoor storage facilities.



A full service transload facility can attract a diverse base of commodities for customers not directly served by rail.

A transload facility will often-times function as a “business incubator” for new industry looking to move into an area, but not yet ready to spend capital on a permanent rail-served facility.

Economic / Industrial Development

Much of the Watsonville – Davenport rail corridor has been fully developed. Many former industrial properties and land in Santa Cruz have been redeveloped into light industrial, office, residential or other non-rail use.

The best opportunities for new economic development initiatives will likely occur in the Watsonville area as under-utilized warehouse space and allocated acreage adjacent to the rail corridor can be marketed to industry needing rail transportation.

The City of Watsonville has identified retention and expansion of their industrial base as one of the key elements of their economic development strategy.¹⁹

Successful development and redevelopment of a rail-served industrial base will require focused marketing and awareness initiatives undertaken by all development stakeholders in the region in partnership with the shortline railroad.

¹⁹ City of Watsonville Economic Development Strategy Executive Summary, March 26, 2008.

Capital and Maintenance Plan

A complete track maintenance survey and report has been proposed by the RTC and will be prepared by an outside engineering firm.

Bridge repair and on-going bridge maintenance expense estimates have already been provided to the RTC.

Pending the results of the track maintenance report, the RTC is proposing a track and structures capital program of approximately \$5 million. These funds will repair specific items in bridge structures and will address any track repair or replacement issues that are discovered.

In 2004, the UP undertook a significant track rehabilitation program between Watsonville and Davenport, replacing 37,000 rail ties, reconstructing several grade crossings, cleaning ditches and applying several thousand tons of rock ballast to improve structural integrity and drainage.²⁰

The shortline railroad will be expected to maintain track and bridge structures at or above their current state of repair or eventual state of repair for freight service after capital investment by the RTC.

Major components to a normalized track maintenance program include:

- Crosstie replacement
- Track surfacing, lining, leveling and ballast replacement
- Vegetation control (canopy and weed encroachment)
- Spot rail replacement
- Bolt tightening on joint bars
- Ditching and drainage
- Bridge Maintenance

It is assumed that all programmed maintenance would be contracted out. Spot maintenance, inspections and management of contractors would be managed by shortline railroad's employees.

²⁰ UP Roadmaster DeWayne Hillman, 10/4/2008.

Types and Timing of Maintenance Items

The final track maintenance report will detail any specific track maintenance items as well as a specific maintenance protocol for the corridor. Until that report is complete, certain assumptions with respect to expected minimum track maintenance requirements have been made, and include:

Track - Crossties

Normal programmed tie replacement for this line would be 2800 – 3000 crossties per year. UP's 2004 track project allows for a lower initial replacement requirement for the first 5 years, so the following schedule could be adopted:

- Years 1-5: Normalized tie replacement program of 1500 crossties / year.
- Years 6 and beyond: Escalating tie replacement program to 2800 ties / year.

Track – Ballast and Surfacing

Normal ballast renewal and “top-dressing” for this line would be 1400 – 1600 tons per year. UP's 2004 track project allows for a lower initial replacement requirement for the first 5 years, so the following schedule could be adopted:

- Years 1-5: Ballast renewal program of 1000 tons / year.
- Years 6 and beyond: Escalating ballast renewal program to 1500 tons / year.

In conjunction with crosstie replacement and ballast renewal, a scheduled program of surfacing will occur as well. “Surfacing” is conducted to restore proper alignment and elevation of the track structure. While specific areas may require a greater frequency of attention, it is reasonable to expect that a rail line of this traffic density should undergo a complete resurfacing over a 10-15 year timeframe, meaning that 2-3 miles of track need to be resurfaced each year.



Properly ballasted and surfaced mainline

Track –Spot Rail Replacement

Spot rail replacement occurs on an as-needed basis. Rail in the corridor, despite its age, is in generally good condition and given an appropriate tie and ballast foundation, will continue to be suitable for the needs to the railroad.

Vegetation Control

The rail corridor is currently treated 3 times per year for weed growth in the track structure. This practice would need to be continued.

Controlling the vegetation canopy (trees, brush, etc...) is generally performed on an as-needed basis.

Ditching and Drainage

Given the topography in which the rail corridor exists, significant attention will need to be given to ensuring the right-of-way has adequate drainage



Vegetation canopy and brush encroachment issues require continued attention to insure they don't effect operations

Bridge Maintenance

Separate engineering studies have been commissioned by the RTC to quantify Bridge CAPEX and ongoing maintenance requirements. The following table illustrates the potential range of bridge maintenance expenses that will be incurred by the shortline railroad:

Table 3: Anticipated Bridge Maintenance Requirements for Shortline Railroad

Identified Annual Bridge Maintenance						
Mile Post	Location	Low	High	Average	Approximate Material Costs	Approximate "Soft" Costs
0.86		\$ 4,300	\$ 5,400	\$ 4,850	\$ 3,153	\$ 1,698
1.06a		\$ 3,600	\$ 4,900	\$ 4,250	\$ 2,763	\$ 1,488
1.06b	Pajaro River Crossing	\$ 5,670	\$ 9,585	\$ 7,628	\$ 4,958	\$ 2,670
1.06c		\$ 1,800	\$ 2,500	\$ 2,150	\$ 1,398	\$ 753
4.45	Watsonville Slough	\$ 1,300	\$ 1,400	\$ 1,350	\$ 878	\$ 473
	Retaining Wall	\$ -	\$ 540	\$ 270	\$ 176	\$ 95
4.87	Harkins Slough	\$ 3,800	\$ 5,000	\$ 4,400	\$ 2,860	\$ 1,540
5.42		\$ 1,000	\$ 1,300	\$ 1,150	\$ 748	\$ 403
5.54		\$ 2,800	\$ 3,500	\$ 3,150	\$ 2,048	\$ 1,103
6.01		\$ 1,800	\$ 2,400	\$ 2,100	\$ 1,365	\$ 735
6.14		\$ 1,000	\$ 1,300	\$ 1,150	\$ 748	\$ 403
6.25		\$ 2,400	\$ 3,500	\$ 2,950	\$ 1,918	\$ 1,033
8.32		\$ 1,000	\$ 1,300	\$ 1,150	\$ 748	\$ 403
8.64a	San Andreas Road	\$ 1,000	\$ 1,400	\$ 1,200	\$ 780	\$ 420
8.64b	San Andreas Road	\$ 2,200	\$ 3,100	\$ 2,650	\$ 1,723	\$ 928
	Retaining Wall	\$ -	\$ 675	\$ 338	\$ 219	\$ 118
9.09	La Selva Beach Trestle	\$ 8,370	\$ 14,985	\$ 11,678	\$ 7,590	\$ 4,087
9.3	Retaining Wall	\$ -	\$ 495	\$ 248	\$ 161	\$ 87
10.45	Seascape Trestle	\$ 4,860	\$ 7,425	\$ 6,143	\$ 3,993	\$ 2,150
11.16		\$ 4,700	\$ 7,600	\$ 6,150	\$ 3,998	\$ 2,153
12.3	State Route 1	\$ 2,100	\$ 3,100	\$ 2,600	\$ 1,690	\$ 910
12.34	Valenica Creek	\$ 4,900	\$ 6,800	\$ 5,850	\$ 3,803	\$ 2,048
12.39	Soquel Drive	\$ 1,300	\$ 1,900	\$ 1,600	\$ 1,040	\$ 560
12.71a	Aptos Creek & Spreckles Drive	\$ 3,600	\$ 4,400	\$ 4,000	\$ 2,600	\$ 1,400
12.71b		\$ 1,700	\$ 2,100	\$ 1,900	\$ 1,235	\$ 665
12.83	Sate Route 1	\$ 3,100	\$ 3,900	\$ 3,500	\$ 2,275	\$ 1,225
14.85	New Brighton Beach Road	\$ 1,000	\$ 1,400	\$ 1,200	\$ 780	\$ 420
15.89a	Capitola Crossing	\$ 1,890	\$ 2,700	\$ 2,295	\$ 1,492	\$ 803
15.89b	Capitola Crossing	\$ 4,455	\$ 6,750	\$ 5,603	\$ 3,642	\$ 1,961
15.89c	Capitola Crossing	\$ 3,375	\$ 5,670	\$ 4,523	\$ 2,940	\$ 1,583
15.89d	Capitola Crossing	\$ 945	\$ 1,350	\$ 1,148	\$ 746	\$ 402
15.89e	Capitola Crossing	\$ 1,080	\$ 1,620	\$ 1,350	\$ 878	\$ 473
17.3	Rodeo Gulch	\$ 4,900	\$ 6,700	\$ 5,800	\$ 3,770	\$ 2,030
18.84	SC Small Craft Harbor	\$ 4,000	\$ 6,100	\$ 5,050	\$ 3,283	\$ 1,768
19.43a	San Lorenzo River	\$ 4,860	\$ 8,505	\$ 6,683	\$ 4,344	\$ 2,339
19.43b	San Lorenzo River	\$ 1,080	\$ 1,755	\$ 1,418	\$ 921	\$ 496
22.29	Moore's Gulch	\$ 6,500	\$ 9,500	\$ 8,000	\$ 5,200	\$ 2,800
23.47	Wilder Creek	\$ 1,000	\$ 1,300	\$ 1,150	\$ 748	\$ 403
23.54	Meder Creek Crossing	\$ 270	\$ 540	\$ 405	\$ 263	\$ 142
26.09	Baldwin Creek	\$ 1,000	\$ 1,300	\$ 1,150	\$ 748	\$ 403
26.55		\$ 1,000	\$ 1,300	\$ 1,150	\$ 748	\$ 403
Total		\$ 105,655	\$ 156,995	\$ 131,325	\$ 85,361	\$ 45,964

Total anticipated on-going track and structures maintenance costs for a shortline operating in the corridor are anticipated between \$375,000 and \$425,000 per year.

Financial Analysis of New Shortline Operations

The following section details initial financial analysis of the three potential transaction scenarios which would create an operating shortline railroad in the corridor. Each analysis includes Income Statement, Balance Sheet, Cash Flow Statement and an Initial Capitalization Worksheet.

Holding Company Operation

Income Statement

Significant assumptions used in developing Holding Company shortline model which are reflected in the Income Statement include:

- Lower permanent headcount as management resources would likely be shared with other neighboring properties.
- Locomotive Equipment assets are not capitalized, rather, they are assigned to the property from current Company stock and the property is assessed a slightly discounted lease rate which is accounted for in Transportation Expense.
- Interest Expense is a function of Termed Senior Debt and in initial Line of Credit.

Santa Cruz Rail Line - "Holding Company" Model						
Income Statement						
		Year 1	Year 2	Year 3	Year 4	Year 5
Headcount		3.75	3.75	3.75	3.75	3.75
Carloads		3,376	3,376	3,376	3,376	3,376
Revenue:						
Linehaul Revenue		\$ 1,079,350	\$ 1,110,912	\$ 1,145,124	\$ 1,179,521	\$ 1,214,954
Non-Linehaul Revenue		-	-	-	-	-
Total Revenues		\$ 1,079,350	\$ 1,110,912	\$ 1,145,124	\$ 1,179,521	\$ 1,214,954
Operating Expenses:						
Transportation	32.8%	\$ 353,857	\$ 361,352	\$ 369,072	\$ 377,023	\$ 385,213
Roadway Maintenance	36.2%	\$ 390,220	\$ 400,996	\$ 413,026	\$ 425,417	\$ 438,179
Equipment Maintenance	4.9%	\$ 52,500	\$ 54,375	\$ 57,094	\$ 59,948	\$ 62,946
General & Administrative	19.7%	\$ 212,813	\$ 219,677	\$ 226,771	\$ 234,104	\$ 241,682
Operating Expenses Before Deprec. & Amtz.	93.5%	\$ 1,009,390	\$ 1,036,400	\$ 1,065,963	\$ 1,096,492	\$ 1,128,021
EBITDA	6.5%	\$ 69,961	\$ 74,511	\$ 79,161	\$ 83,029	\$ 86,933
Interest Expense	1.8%	\$ 18,916	\$ 13,026	\$ 11,983	\$ 10,857	\$ 9,640
Depreciation and Amortization Expense	2.5%	27,000	27,000	27,000	27,000	27,000
Total Operating Expenses	97.8%	\$ 1,055,305	\$ 1,076,426	\$ 1,104,946	\$ 1,134,349	\$ 1,164,660
Net Income	2.2%	\$ 24,045	\$ 34,485	\$ 40,178	\$ 45,173	\$ 50,293

Balance Sheet

Santa Cruz Rail Line - Holding Company Model Balance Sheet						
Assets:	Starting Balances	Year 1	Year 2	Year 3	Year 4	Year 5
Current Assets:						
Cash	\$ 249,000	\$ 235,212	\$ 281,619	\$ 330,973	\$ 387,815	\$ 446,676
Accounts Receivable		89,946	92,576	95,427	98,293	101,246
Other Current Assets	\$ 1,500	-	-	-	-	-
Total Current Assets	\$ 250,500	\$ 325,157	\$ 374,195	\$ 426,400	\$ 486,109	\$ 547,922
Fixed Assets:						
Property, Plant, Equip.(at cost)	\$ 123,670	\$ 123,670	\$ 123,670	\$ 123,670	\$ 123,670	\$ 123,670
Accumulated Dep./ Amort.		22,400	44,800	67,200	89,600	112,000
Net Prop./ Plant / Equip	\$ 123,670	\$ 101,270	\$ 78,870	\$ 56,470	\$ 34,070	\$ 11,670
Capital Leases	\$ -	-	-	-	-	-
Intangibles / Goodwill	\$ 71,109	71,109	71,109	71,109	71,109	71,109
Amortization Of Intangibles		4,600	9,200	13,800	18,400	23,000
Net Intangibles	\$ 71,109	\$ 66,509	\$ 61,909	\$ 57,309	\$ 52,709	\$ 48,109
Deposits	\$ -	-	-	-	-	-
Total Assets	\$ 445,279	\$ 492,937	\$ 514,974	\$ 540,179	\$ 572,888	\$ 607,702
Liabilities:						
Accounts Payable	\$ -	\$ 87,998	\$ 92,666	\$ 99,259	\$ 102,247	\$ 107,206
Notes Payable	\$ -	-	-	-	-	-
Line of Credit	\$ -	-	-	-	-	-
Current Portion of LT Debt	\$ -	12,073	13,039	14,082	15,209	16,426
Current Portion of Subordinated Debt	\$ -	-	-	-	-	-
Capital Leases- Current portion	\$ -	-	-	-	-	-
Total Current Liabilities	\$ -	\$ 100,071	\$ 105,706	\$ 113,341	\$ 117,456	\$ 123,632
Long-Term Senior Debt	\$ 174,901	\$ 150,755	\$ 136,749	\$ 121,624	\$ 105,288	\$ 87,646
Subordinated Debt	\$ -	-	-	-	-	-
Convertible Debt	\$ -	-	-	-	-	-
LT Capital Leases	\$ -	-	-	-	-	-
Total Long-Term Liabilities	\$ 174,901	\$ 150,755	\$ 136,749	\$ 121,624	\$ 105,288	\$ 87,646
Total Liabilities	\$ 174,901	\$ 250,825	\$ 242,455	\$ 234,965	\$ 222,744	\$ 211,278
Shareholders' Equity:						
Common Stock	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000	\$ 200,000
Preferred Stock	\$ -	-	-	-	-	-
Capital Surplus	\$ -	-	-	-	-	-
Retained Earnings	\$ -	42,111	72,519	105,214	150,144	196,424
Total Equity	\$ 200,000	\$ 242,111	\$ 272,519	\$ 305,214	\$ 350,144	\$ 396,424
Total Liabilities and Equity	\$ 374,901	\$ 492,936	\$ 514,974	\$ 540,179	\$ 572,888	\$ 607,702
Number of Common Shares Issued	100,000	100,000	100,000	100,000	100,000	100,000
Per Share Equity	\$ 2.00	\$ 2.42	\$ 2.73	\$ 3.05	\$ 3.50	\$ 3.96

Cash Flow Statement

Santa Cruz Rail Line - Holding Company Model					
Cash Flow Statements					
	Year 1	Year 2	Year 3	Year 4	Year 5
Cash at Beginning of Period	\$ 249,000	\$ 235,212	\$ 281,619	\$ 330,973	\$ 387,815
EBITDA	69,961	74,511	79,161	83,029	86,933
Working Capital Changes Increase/(Decrease)	1,948	(2,039)	(3,741)	(122)	(2,007)
Net Cash From/(Used By) Operations	\$ 71,909	\$ 72,473	\$ 75,420	\$ 82,908	\$ 84,926
Cash From Financing Activities					
Cash From (Used By) Financing Activities-Interest Pmt.	\$ (18,916)	\$ (13,026)	\$ (11,983)	\$ (10,857)	\$ (9,640)
Cash From (Used By) Financing Activities-Principal Pmt.	(66,781)	(13,039)	(14,082)	(15,209)	(16,426)
Net Cash From/(Used By) Financing	\$ (85,697)	\$ (26,065)	\$ (26,065)	\$ (26,065)	\$ (26,065)
Cash From Investments					
Cash (Used By) Capital Exp. for Facilities*	\$ -	\$ -	\$ -	\$ -	\$ -
Cash (Used By) Capital Exp. for Equipment*	-	-	-	-	-
Cash (Used By) Capital Exp. for Maintenance of Way	-	-	-	-	-
Cash (Used By) Capital Exp. for Other Purposes	-	-	-	-	-
Cash (Used By) Principal Repayment	-	-	-	-	-
Net Cash From/(Used By) Investments	\$ -	\$ -	\$ -	\$ -	\$ -
Cash From Investors/Owners/	\$ -	\$ -	\$ -	\$ -	\$ -
Cash (Distributed To) Investors/Owners	-	-	-	-	-
Net Cash From/(Distributed To) Inv/Owners	\$ -	\$ -	\$ -	\$ -	\$ -
Income Tax Benefit/(Expense)	\$ -	\$ -	\$ -	\$ -	\$ -
Net Cash Flow (after-taxes)	\$ (13,788)	\$ 46,407	\$ 49,354	\$ 56,842	\$ 58,861
Cash at End of Period	\$ 235,212	\$ 281,619	\$ 330,973	\$ 387,815	\$ 446,676
Cash Flow / Investment Statistics					
Working Capital	\$ 250,500	\$ 225,087	\$ 268,489	\$ 313,059	\$ 368,653
EBITDA	69,961	74,511	79,161	83,029	86,933
Implied Franchise Value @ EBITDA multiple of 5.0	349,803	372,557	395,805	415,147	434,665

Initial Capitalization Worksheet

Significant assumptions used in developing Holding Company shortline model which are reflected in the Capitalization Worksheet include:

- Senior Debt is calculated at a multiple of 2.5x's EBITDA. Equity Cash and Line of Credit comprise balance of initial capitalization.

Santa Cruz Rail Line - Holding Company Model						
Capital, Depreciation and Amortization Worksheet						
Financing Sources and Uses of Funds						
Sources of Funding:						
Common Equity - Cash Contribution					\$	200,000
Common Equity - Other Equity Contribution						-
Common Equity - Investor's Cash Contribution						-
Long-Term Subordinated Debt						-
Long-Term Senior Debt						174,901
Working Capital Credit Line		<i>Credit line as a % of A/R</i>	70%	\$	94,400	
		<i>and as a % of inventory</i>	65%		-	
		<i>Nominal line</i>		\$	94,400	54,708
Total Sources of Funding					\$	429,609
Uses of Funding:						
Organization and Acquisition Expenses					\$	71,109
Franchise Acquisition						-
Equipment Acquired from Seller						-
Track Materials and Inventories Acquired from Seller						-
Initial Capital Expenditures						109,500
Initial Working Capital Requirements						249,000
						<i>90 days cash operating expenses</i>
Total Uses of Funding					\$	429,609
Line of Credit Worksheet						
Line of Credit	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Annual Interest Rate	9.0%					
Drawdowns		54,708				
Interest Payments		4,924	-	-	-	-
Principal Reductions		54,708	-	-	-	-
Ending Principal		\$ -	\$ -	\$ -	\$ -	\$ -
Term Debt Worksheet						
Senior Debt	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ 174,901	\$ 174,901	\$ 162,828	\$ 149,789	\$ 135,706	\$ 120,497
Term (years)	10					
Annual Interest Rate	8.0%					
Annual Payment	26,065	26,065	26,065	26,065	26,065	26,065
Interest Portion		13,992	13,026	11,983	10,857	9,640
Principal Portion		12,073	13,039	14,082	15,209	16,426
Ending Principal		\$ 162,828	\$ 149,789	\$ 135,706	\$ 120,497	\$ 104,072
Subordinated Debt	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Term (years)	7					
Annual Interest Rate	10.0%					
Annual Payment	-	-	-	-	-	-
Interest Portion		-	-	-	-	-
Principal Portion		-	-	-	-	-
Ending Principal		\$ -	\$ -	\$ -	\$ -	\$ -
Debt Summaries						
	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Total interest expense		\$ 18,916	\$ 13,026	\$ 11,983	\$ 10,857	\$ 9,640
Principal reductions		66,781	13,039	14,082	15,209	16,426

Notes

Privately Owned Stand-Alone Shortline Operation

Income Statement

Significant assumptions used in developing Stand Alone shortline model which are reflected in the Income Statement include:

- Headcount reflects self-contained operation.
- Locomotive Equipment assets are capitalized accounting for higher Depreciation.
- Interest Expense is a function of Termed Senior Debt and in initial Line of Credit.

Santa Cruz Rail Line - Stand-Alone: Capitalize Equipment						
Income Statement						
		Year 1	Year 2	Year 3	Year 4	Year 5
Headcount		5.00	5.00	5.00	5.00	5.00
Carloads		3,376	3,376	3,376	3,376	3,376
Revenue:						
Linehaul Revenue		\$ 1,079,350	\$ 1,110,912	\$ 1,145,124	\$ 1,179,521	\$ 1,214,954
Non-Linehaul Revenue		-	-	-	-	-
Total Revenues		\$ 1,079,350	\$ 1,110,912	\$ 1,145,124	\$ 1,179,521	\$ 1,214,954
Operating Expenses:						
Transportation	23.1%	\$ 249,832	\$ 257,327	\$ 265,047	\$ 272,998	\$ 281,188
Roadway Maintenance	39.3%	\$ 423,970	\$ 435,759	\$ 448,831	\$ 462,296	\$ 476,165
Equipment Maintenance	4.9%	\$ 52,500	\$ 54,375	\$ 57,094	\$ 59,948	\$ 62,946
General & Administrative	26.8%	\$ 288,750	\$ 297,893	\$ 307,333	\$ 317,082	\$ 327,151
Operating Expenses Before Deprec. & Amtz.	94.0%	\$ 1,015,052	\$ 1,045,353	\$ 1,078,305	\$ 1,112,325	\$ 1,147,450
EBITDA	6.0%	\$ 64,298	\$ 65,558	\$ 66,819	\$ 67,196	\$ 67,504
Interest Expense	2.6%	\$ 27,785	\$ 17,724	\$ 16,020	\$ 14,164	\$ 12,144
Depreciation and Amortization Expense	7.1%	77,000	77,000	77,000	77,000	77,000
Total Operating Expenses	103.8%	\$ 1,119,837	\$ 1,140,077	\$ 1,171,325	\$ 1,203,490	\$ 1,236,594
Net Income	-3.8%	\$ (40,487)	\$ (29,166)	\$ (26,201)	\$ (23,968)	\$ (21,640)

Balance Sheet

Santa Cruz Rail Line - Stand Alone Model						
Balance Sheet						
Assets:	Starting Balances	Year 1	Year 2	Year 3	Year 4	Year 5
Current Assets:						
Cash	\$ 250,000	\$ 175,694	\$ 201,744	\$ 227,309	\$ 256,893	\$ 284,857
Accounts Receivable		89,946	92,576	95,427	98,293	101,246
Other Current Assets	\$ 1,500	-	-	-	-	-
Total Current Assets	\$ 251,500	\$ 265,640	\$ 294,319	\$ 322,736	\$ 355,187	\$ 386,103
Fixed Assets:						
Property, Plant, Equip.(at cost)	\$ 859,500	\$ 859,500	\$ 859,500	\$ 859,500	\$ 859,500	\$ 859,500
Accumulated Dep./ Amort.		72,400	144,800	217,200	289,600	362,000
Net Prop./ Plant / Equip	\$ 859,500	\$ 787,100	\$ 714,700	\$ 642,300	\$ 569,900	\$ 497,500
Capital Leases	\$ -	-	-	-	-	-
Intangibles / Goodwill	\$ 80,250	80,250	80,250	80,250	80,250	80,250
Amortization Of Intangibles		4,600	9,200	13,800	18,400	23,000
Net Intangibles	\$ 80,250	\$ 75,650	\$ 71,050	\$ 66,450	\$ 61,850	\$ 57,250
Deposits	\$ -	-	-	-	-	-
Total Assets	\$ 1,191,250	\$ 1,128,390	\$ 1,080,069	\$ 1,031,486	\$ 986,937	\$ 940,853
Liabilities:						
Accounts Payable	\$ -	\$ 88,491	\$ 93,467	\$ 100,408	\$ 103,723	\$ 109,053
Notes Payable	\$ -	-	-	-	-	-
Line of Credit	\$ -	-	-	-	-	-
Current Portion of LT Debt	\$ -	11,096	11,984	12,943	13,978	15,096
Current Portion of Subordinated Debt	\$ -	6,777	7,455	8,201	9,021	9,923
Capital Leases- Current portion	\$ -	-	-	-	-	-
Total Current Liabilities	\$ -	\$ 106,365	\$ 112,906	\$ 121,551	\$ 126,722	\$ 134,072
Long-Term Senior Debt	\$ 160,745	\$ 138,553	\$ 125,681	\$ 111,780	\$ 96,767	\$ 80,552
Subordinated Debt	\$ 64,298	50,743	42,610	33,664	23,824	12,999
Convertible Debt	\$ -	-	-	-	-	-
LT Capital Leases	\$ -	-	-	-	-	-
Total Long-Term Liabilities	\$ 225,043	\$ 189,296	\$ 168,292	\$ 145,444	\$ 120,590	\$ 93,551
Total Liabilities	\$ 225,043	\$ 295,661	\$ 281,198	\$ 266,995	\$ 247,312	\$ 227,623
Shareholders' Equity:						
Common Stock	\$ 850,000	\$ 850,000	\$ 850,000	\$ 850,000	\$ 850,000	\$ 850,000
Preferred Stock	\$ -	-	-	-	-	-
Capital Surplus	\$ -	-	-	-	-	-
Retained Earnings	\$ -	(17,271)	(51,128)	(85,509)	(110,376)	(136,769)
Total Equity	\$ 850,000	\$ 832,729	\$ 798,872	\$ 764,491	\$ 739,624	\$ 713,231
Total Liabilities and Equity	\$ 1,075,043	\$ 1,128,390	\$ 1,080,070	\$ 1,031,486	\$ 986,936	\$ 940,854
Number of Common Shares Issued	100,000	100,000	100,000	100,000	100,000	100,000
Per Share Equity	\$ 8.50	\$ 8.33	\$ 7.99	\$ 7.64	\$ 7.40	\$ 7.13

Cash Flow Statement

Santa Cruz Rail Line - Stand Alone Model

Cash Flow Statements

	Year 1	Year 2	Year 3	Year 4	Year 5
Cash at Beginning of Period	\$ 250,000	\$ 175,694	\$ 201,744	\$ 227,309	\$ 256,893
EBITDA	64,298	65,558	66,819	67,196	67,504
Working Capital Changes Increase/(Decrease)	1,455	(2,346)	(4,090)	(449)	(2,377)
Net Cash From/(Used By) Operations	\$ 65,753	\$ 63,213	\$ 62,728	\$ 66,747	\$ 65,127
Cash From Financing Activities					
Cash From (Used By) Financing Activities-Interest Pmt.	\$ (27,785)	\$ (17,724)	\$ (16,020)	\$ (14,164)	\$ (12,144)
Cash From (Used By) Financing Activities-Principal Pmt.	(112,274)	(19,439)	(21,143)	(22,999)	(25,019)
Net Cash From/(Used By) Financing	\$ (140,059)	\$ (37,163)	\$ (37,163)	\$ (37,163)	\$ (37,163)
Cash From Investments					
Cash (Used By) Capital Exp. for Facilities*	\$ -	\$ -	\$ -	\$ -	\$ -
Cash (Used By) Capital Exp. for Equipment*	-	-	-	-	-
Cash (Used By) Capital Exp. for Maintenance of Way	-	-	-	-	-
Cash (Used By) Capital Exp. for Other Purposes	-	-	-	-	-
Cash (Used By) Principal Repayment	-	-	-	-	-
Net Cash From/(Used By) Investments	\$ -	\$ -	\$ -	\$ -	\$ -
Cash From Investors/Owners/	\$ -	\$ -	\$ -	\$ -	\$ -
Cash (Distributed To) Investors/Owners	-	-	-	-	-
Net Cash From/(Distributed To) Inv/Owners	\$ -	\$ -	\$ -	\$ -	\$ -
Income Tax Benefit/(Expense)	\$ -	\$ -	\$ -	\$ -	\$ -
Net Cash Flow (after-taxes)	\$ (74,306)	\$ 26,050	\$ 25,566	\$ 29,584	\$ 27,964
Cash at End of Period	\$ 175,694	\$ 201,744	\$ 227,309	\$ 256,893	\$ 284,857
Cash Flow / Investment Statistics					
Working Capital	\$ 251,500	\$ 159,275	\$ 181,414	\$ 201,185	\$ 228,464
EBITDA		64,298	65,558	66,819	67,196
Implied Franchise Value @ EBITDA multiple of 5.0		321,490	327,792	334,093	335,980
					337,519

Initial Capitalization Worksheet

Significant assumptions used in developing Holding Company shortline model which are reflected in the Capitalization Worksheet include:

- Senior Debt is calculated at a multiple of 2.5x's EBITDA. A small Subordinated Debt piece is added to Capitalization along with Equity Cash and Line of Credit..

Santa Cruz Rail Line - Stand Alone Model						
Capital, Depreciation and Amortization Worksheet						
Financing Sources and Uses of Funds						
Sources of Funding:						
Common Equity - Cash Contribution					\$	850,000
Common Equity - Other Equity Contribution						-
Common Equity - Investor's Cash Contribution						-
Long-Term Subordinated Debt						64,298
Long-Term Senior Debt						160,745
Working Capital Credit Line		<i>Credit line as a % of A/R</i>	<i>70%</i>	\$	94,400	
		<i>and as a % of inventory</i>	<i>65%</i>		-	
		<i>Nominal line</i>		\$	94,400	94,400
Total Sources of Funding						\$ 1,169,443
Uses of Funding:						
Organization and Acquisition Expenses					\$	80,250
Franchise Acquisition						-
Equipment Acquired from Seller						-
Track Materials and Inventories Acquired from Seller						-
Initial Capital Expenditures						859,500
Initial Working Capital Requirements						250,000
						<i>90 days cash operating expenses</i>
Total Uses of Funding						\$ 1,189,750
Line of Credit Worksheet						
Line of Credit	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Annual Interest Rate	9.0%					
Drawdowns		94,400				
Interest Payments		8,496	-	-	-	-
Principal Reductions		94,400	-	-	-	-
Ending Principal		\$ -	\$ -	\$ -	\$ -	\$ -
Term Debt Worksheet						
Senior Debt	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ 160,745	\$ 160,745	\$ 149,649	\$ 137,665	\$ 124,722	\$ 110,745
Term (years)	10					
Annual Interest Rate	8.0%					
Annual Payment	23,956	23,956	23,956	23,956	23,956	23,956
Interest Portion		12,860	11,972	11,013	9,978	8,860
Principal Portion		11,096	11,984	12,943	13,978	15,096
Ending Principal		\$ 149,649	\$ 137,665	\$ 124,722	\$ 110,745	\$ 95,648
Subordinated Debt	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ 64,298	\$ 64,298	\$ 57,521	\$ 50,066	\$ 41,865	\$ 32,844
Term (years)	7					
Annual Interest Rate	10.0%					
Annual Payment	13,207	13,207	13,207	13,207	13,207	13,207
Interest Portion		6,430	5,752	5,007	4,186	3,284
Principal Portion		6,777	7,455	8,201	9,021	9,923
Ending Principal		\$ 57,521	\$ 50,066	\$ 41,865	\$ 32,844	\$ 22,922
Debt Summaries						
	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Total interest expense		\$ 27,785	\$ 17,724	\$ 16,020	\$ 14,164	\$ 12,144
Principal reductions		112,274	19,439	21,143	22,999	25,019

Notes

Publically Owned Shortline Operation

Income Statement

Significant assumptions used in developing Publically Owned shortline model which are reflected in the Income Statement include:

- Headcount reflects self-contained operation.
- Locomotive Equipment assets are capitalized accounting for higher Depreciation.
- Shortline receives all freight and property revenues.
- Interest Expense is a function of Termed Senior Debt and in initial Line of Credit.

Santa Cruz Rail Line - SCCRTC Start-up						
Income Statement						
		Year 1	Year 2	Year 3	Year 4	Year 5
Headcount		5.00	5.00	5.00	5.00	5.00
Carloads		3,376	3,376	3,376	3,376	3,376
Revenue:						
Linehaul Revenue		\$ 1,079,350	\$ 1,110,912	\$ 1,145,124	\$ 1,179,521	\$ 1,214,954
Non-Linehaul Revenue		125,000	128,750	132,613	136,591	140,689
Total Revenues		\$ 1,204,350	\$ 1,239,662	\$ 1,277,736	\$ 1,316,112	\$ 1,355,642
Operating Expenses:						
Transportation	20.7%	\$ 249,832	\$ 257,327	\$ 265,047	\$ 272,998	\$ 281,188
Roadway Maintenance	35.2%	\$ 423,970	\$ 435,759	\$ 448,831	\$ 462,296	\$ 476,165
Equipment Maintenance	4.4%	\$ 52,500	\$ 54,375	\$ 57,094	\$ 59,948	\$ 62,946
General & Administrative	25.8%	\$ 310,794	\$ 320,589	\$ 330,720	\$ 341,171	\$ 351,962
Operating Expenses Before Deprec. & Amtz.	86.1%	\$ 1,037,096	\$ 1,068,050	\$ 1,101,692	\$ 1,136,414	\$ 1,172,261
EBITDA	13.9%	\$ 167,255	\$ 171,612	\$ 176,045	\$ 179,698	\$ 183,381
Interest Expense	3.0%	\$ 36,685	\$ 27,822	\$ 25,401	\$ 22,834	\$ 20,114
Depreciation and Amortization Expense	6.4%	77,000	77,000	77,000	77,000	77,000
Total Operating Expenses	95.6%	\$ 1,150,780	\$ 1,172,872	\$ 1,204,092	\$ 1,236,248	\$ 1,269,375
Net Income	4.4%	\$ 53,570	\$ 66,790	\$ 73,644	\$ 79,864	\$ 86,267

Balance Sheet

Santa Cruz Rail Line - SCCRTC Start-Up Balance Sheet						
Assets:	Starting Balances	Year 1	Year 2	Year 3	Year 4	Year 5
Current Assets:						
Cash	\$ 256,000	\$ 264,465	\$ 365,762	\$ 469,717	\$ 581,056	\$ 694,116
Accounts Receivable		100,363	103,305	106,478	109,676	112,970
Other Current Assets	\$ 1,500	-	-	-	-	-
Total Current Assets	\$ 257,500	\$ 364,827	\$ 469,067	\$ 576,195	\$ 690,732	\$ 807,086
Fixed Assets:						
Property, Plant, Equip.(at cost)	\$ 859,500	\$ 859,500	\$ 859,500	\$ 859,500	\$ 859,500	\$ 859,500
Accumulated Dep./ Amort.		72,400	144,800	217,200	289,600	362,000
Net Prop./ Plant / Equip	\$ 859,500	\$ 787,100	\$ 714,700	\$ 642,300	\$ 569,900	\$ 497,500
Capital Leases	\$ -	-	-	-	-	-
Intangibles / Goodwill	\$ 80,250	80,250	80,250	80,250	80,250	80,250
Amortization Of Intangibles		4,600	9,200	13,800	18,400	23,000
Net Intangibles	\$ 80,250	\$ 75,650	\$ 71,050	\$ 66,450	\$ 61,850	\$ 57,250
Deposits	\$ -	-	-	-	-	-
Total Assets	\$ 1,197,250	\$ 1,227,577	\$ 1,254,817	\$ 1,284,945	\$ 1,322,482	\$ 1,361,836
Liabilities:						
Accounts Payable	\$ -	\$ 90,413	\$ 95,496	\$ 102,586	\$ 105,970	\$ 111,411
Notes Payable	\$ -	-	-	-	-	-
Line of Credit	\$ -	-	-	-	-	-
Current Portion of LT Debt	\$ -	38,068	40,352	42,773	45,339	48,060
Current Portion of Subordinated Debt	\$ -	-	-	-	-	-
Capital Leases- Current portion	\$ -	-	-	-	-	-
Total Current Liabilities	\$ -	\$ 128,481	\$ 135,848	\$ 145,359	\$ 151,309	\$ 159,471
Long-Term Senior Debt	\$ 501,764	\$ 425,628	\$ 382,992	\$ 337,798	\$ 289,892	\$ 239,112
Subordinated Debt	\$ -	-	-	-	-	-
Convertible Debt	\$ -	-	-	-	-	-
LT Capital Leases	\$ -	-	-	-	-	-
Total Long-Term Liabilities	\$ 501,764	\$ 425,628	\$ 382,992	\$ 337,798	\$ 289,892	\$ 239,112
Total Liabilities	\$ 501,764	\$ 554,109	\$ 518,840	\$ 483,157	\$ 441,201	\$ 398,583
Shareholders' Equity:						
Common Stock	\$ 600,000	\$ 600,000	\$ 600,000	\$ 600,000	\$ 600,000	\$ 600,000
Preferred Stock	\$ -	-	-	-	-	-
Capital Surplus	\$ -	-	-	-	-	-
Retained Earnings	\$ -	73,469	135,977	201,788	281,280	363,253
Total Equity	\$ 600,000	\$ 673,469	\$ 735,977	\$ 801,788	\$ 881,280	\$ 963,253
Total Liabilities and Equity	\$ 1,101,764	\$ 1,227,578	\$ 1,254,817	\$ 1,284,945	\$ 1,322,481	\$ 1,361,836
Number of Common Shares Issued	100,000	100,000	100,000	100,000	100,000	100,000
Per Share Equity	\$ 6.00	\$ 6.73	\$ 7.36	\$ 8.02	\$ 8.81	\$ 9.63

Cash Flow Statement

Santa Cruz Rail Line - SCCRTC Start-up					
Cash Flow Statements					
	Year 1	Year 2	Year 3	Year 4	Year 5
Cash at Beginning of Period	\$ 256,000	\$ 264,465	\$ 365,762	\$ 469,717	\$ 581,056
EBITDA	167,255	171,612	176,045	179,698	183,381
Working Capital Changes Increase/(Decrease)	9,950	(2,141)	(3,917)	(186)	(2,147)
Net Cash From/(Used By) Operations	\$ 177,204	\$ 169,471	\$ 172,128	\$ 179,512	\$ 181,234
Cash From Financing Activities					
Cash From (Used By) Financing Activities-Interest Pmt.	\$ (36,685)	\$ (27,822)	\$ (25,401)	\$ (22,834)	\$ (20,114)
Cash From (Used By) Financing Activities-Principal Pmt.	(132,054)	(40,352)	(42,773)	(45,339)	(48,060)
Net Cash From/(Used By) Financing	\$ (168,739)	\$ (68,174)	\$ (68,174)	\$ (68,174)	\$ (68,174)
Cash From Investments					
Cash (Used By) Capital Exp. for Facilities*	\$ -	\$ -	\$ -	\$ -	\$ -
Cash (Used By) Capital Exp. for Equipment*	-	-	-	-	-
Cash (Used By) Capital Exp. for Maintenance of Way	-	-	-	-	-
Cash (Used By) Capital Exp. for Other Purposes	-	-	-	-	-
Cash (Used By) Principal Repayment	-	-	-	-	-
Net Cash From/(Used By) Investments	\$ -	\$ -	\$ -	\$ -	\$ -
Cash From Investors/Owners/	\$ -	\$ -	\$ -	\$ -	\$ -
Cash (Distributed To) Investors/Owners	-	-	-	-	-
Net Cash From/(Distributed To) Inv/Owners	\$ -	\$ -	\$ -	\$ -	\$ -
Income Tax Benefit/(Expense)	\$ -	\$ -	\$ -	\$ -	\$ -
Net Cash Flow (after-taxes)	\$ 8,465	\$ 101,297	\$ 103,955	\$ 111,339	\$ 113,060
Cash at End of Period	\$ 264,465	\$ 365,762	\$ 469,717	\$ 581,056	\$ 694,116
Cash Flow / Investment Statistics					
	Year 1	Year 2	Year 3	Year 4	Year 5
Working Capital	\$ 257,500	\$ 236,347	\$ 333,219	\$ 430,836	\$ 539,423
EBITDA	167,255	171,612	176,045	179,698	183,381
Implied Franchise Value @ EBITDA multiple of 5.0	836,273	858,059	880,223	898,492	916,904

Initial Capitalization Worksheet

Significant assumptions used in developing Holding Company shortline model which are reflected in the Capitalization Worksheet include:

- Lower interest costs on Senior Debt and Line of Credit vs. Private companies.
- Senior Debt represents a 3.0x's multiple to EBITDA. It could be configured higher to perhaps cover entire capitalization requirements.

Santa Cruz Rail Line						
Capital, Depreciation and Amortization Worksheet						
Financing Sources and Uses of Funds						
Sources of Funding:						
Common Equity - Cash Contribution						\$ 600,000
Common Equity - Other Equity Contribution						-
Common Equity - Investor's Cash Contribution						-
Long-Term Subordinated Debt						-
Long-Term Senior Debt						501,764
Working Capital Credit Line		<i>Credit line as a % of A/R</i>	70%	\$ 105,400		
		<i>and as a % of inventory</i>	65%	-		
		<i>Nominal line</i>		\$ 105,400		93,987
Total Sources of Funding						\$ 1,195,750
Uses of Funding:						
Organization and Acquisition Expenses						\$ 80,250
Franchise Acquisition						-
Equipment Acquired from Seller						-
Track Materials and Inventories Acquired from Seller						-
Initial Capital Expenditures						859,500
Initial Working Capital Requirements					<i>90 days cash operating expenses</i>	256,000
Total Uses of Funding						\$ 1,195,750
Line of Credit Worksheet						
Line of Credit	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Annual Interest Rate	7.0%					
Drawdowns		93,987				
Interest Payments		6,579	-	-	-	-
Principal Reductions		93,987	-	-	-	-
Ending Principal	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Term Debt Worksheet						
Senior Debt	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ 501,764	\$ 501,764	\$ 463,696	\$ 423,344	\$ 380,571	\$ 335,232
Term (years)	10					
Annual Interest Rate	6.0%					
Annual Payment	68,174	68,174	68,174	68,174	68,174	68,174
Interest Portion		30,106	27,822	25,401	22,834	20,114
Principal Portion		38,068	40,352	42,773	45,339	48,060
Ending Principal	\$ 463,696	\$ 423,344	\$ 380,571	\$ 335,232	\$ 287,172	
Subordinated Debt	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Beginning Principal Amount	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Term (years)	7					
Annual Interest Rate	10.0%					
Annual Payment	-	-	-	-	-	-
Interest Portion		-	-	-	-	-
Principal Portion		-	-	-	-	-
Ending Principal	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Debt Summaries						
	Start-Up	Year 1	Year 2	Year 3	Year 4	Year 5
Total interest expense		\$ 36,685	\$ 27,822	\$ 25,401	\$ 22,834	\$ 20,114
Principal reductions		132,054	40,352	42,773	45,339	48,060

Notes